

ADMINISTRATIVE PROCEEDING  
FILE NO. 3-5881

UNITED STATES OF AMERICA  
Before the  
SECURITIES AND EXCHANGE COMMISSION

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In the Matter of	:
FIRST MULTIFUND ADVISORY CORP.	:
MILTON MOUND	:

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INITIAL DECISION

Washington, D.C.  
December 29, 1982

Irving Schiller  
Administrative Law Judge

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APPEARANCES:

Phillip D. Parker and Nicholas  
F. Coscia for the Division of  
Enforcement.

Milton Mound, Esq. for First  
Multifund Advisory Corp. and  
pro se.

BEFORE:

Irving Schiller  
Administrative Law Judge

THE PROCEEDING

This public proceeding was initiated by an Order of the Commission dated March 5, 1980 (Order under Section 15(b) of the Securities Exchange Act of 1934 (Exchange Act) and Section 9(b) of the Investment Company Act of 1940 (1940 Act) to determine whether First Multifund Advisory Corp., (FMAC), Milton Mound (Mound) and eight other individual respondents wilfully violated or wilfully aided and abetted violations of various securities laws and regulations thereunder and the remedial action, if any, that may be appropriate in the public interest.<sup>1/</sup>

The Order, in essence, charges that respondents FMAC and Mound during the period between 1974 and 1979 wilfully violated and wilfully aided and abetted violations of Section 5 and 17(a) of the Securities Act of 1933 (Securities Act), Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder, Sections 15(c), 12(d)(1)(A)(i) and 30(a)(b) and (d) of the 1940 Act and Rule 22c-1 promulgated thereunder, and Section 206 of the Investment Advisers Act of 1940 (Advisers Act).<sup>2/</sup>

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<sup>1/</sup> The Order alleges wilfull violations against the following eight respondents who have submitted Offers of Settlement which the Commission has determined to accept: James F. Bender(Bender), M. Lester Mendall(Mendall), I.I. Rabi (Rabi), Robert G. Stephens, Jr.(Stephens), Elliot B. Strauss(Strauss), Aaron Warner(Warner), Norman D. Waters(Waters). Exchange Act Release 18977 dated August 18, 1982, 25 SEC Docket, 1492 and Kurt I. Lewin, Securities Exchange Act Release 19196 dated November 1, 1982, 26 SEC Docket 843.

<sup>2/</sup> The Division in its proposed findings of fact and conclusions of law, states it does not address violations of Section 5 of the Securities Act and Sections 12(d)(1)A(1)(i) and 30(a) and (b) of the 1940 Act. Pursuant to Section 16(d) of the Commission's Rules of Practice the violations, as alleged, of the foregoing Sections are regarded as waived and are hereby dismissed.

After appropriate notice evidentiary hearings were held in Washington, D.C. and New York City, New York commencing on July 15, 1980 and concluded on February 25, 1982. Proposed findings of fact, conclusions of law and brief was filed by the Division of Enforcement (Division). Respondents FMAC and Mound did not file proposed findings of facts or briefs. As indicated in note 2 supra, the cases against eight of the respondents charged in the Order with a variety of violations have been concluded. Accordingly, any findings that will necessarily be made herein, which may relate to the aforesaid respondents in light of their involvement in the conduct and activities which are the subject of charges against the remaining two respondents, are not to be considered findings against the said eight respondents whose cases have been determined by the Commission.<sup>3/</sup>

The findings and conclusions herein are based upon the record and upon observation of the witnesses. Preponderance of the evidence is the standard of proof applied.

### The Respondents

Respondent FMAC is registered with the Commission both as a broker-dealer and investment adviser. FMAC acted as the investment adviser to and broker-dealer for First Multifund for Daily Income, Inc. (FMDI) a registered investment company and acted in the same capacities for First Multifund of America, Inc. also a registered investment company.

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3/ See fn. 1/ supra.

Respondent Mound, an attorney is the majority stockholder and chief executive officer of FMAC. Mound also served as chief executive officer and director of both FMDI and FMA (hereinafter sometimes referred to as "the funds") from the inception of each of the investment companies until March 1979.

### The Funds

FMA first registered with the Commission in 1966 under Section 8(a) of the 1940 Act as an open-end, diversified, management investment company.<sup>4/</sup> From its inception until 1979 FMA invested substantially all of its assets in shares of other investment companies and was generally known as a "fund of funds". FMA invested in so-called "load" funds and in "no load" funds.<sup>5/</sup> Pursuant to a management agreement, which was extended annually by FMA's directors, FMAC selected, supervised and managed the investment of the assets of FMA. In addition, FMAC acted as FMA's principal broker in buying shares of load funds for the latter's portfolio for which FMAC received commissions paid by the underwriters of the load funds in which FMA invested. In a reorganization in November 1979, substantially all of the assets of FMA were exchanged for shares of Oppenheimer Special Fund, Inc.<sup>6/</sup>

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<sup>4/</sup> An open-end management investment company is defined in Section 5(a)(1) of the 1940 Act as one which offers for sale redeemable securities.

<sup>5/</sup> A "load" fund is one which requires purchasers of its shares to pay a commission or sales load at the time of acquisition. A "no load" fund makes no charge for the acquisition of its shares. In the "no load" fund the purchaser pays only the net asset value of the fund's shares at the time of acquisition.

<sup>6/</sup> On November 18, 1982 the Commission issued an order pursuant to Section 8(f) of the 1940 Act declaring that FMA ceased to be an investment company as defined in the Act. (Investment Company Act Release No. 12827; 26 SEC Docket 1109).

FMDI first registered with the Commission in 1974 under Section 8(a) of the 1940 Act as an open-end, diversified management investment company. From its inception until 1979 FMDI invested substantially all of its assets in certificates of deposit issued by commercial banks and other debt instruments and was generally known as a "money market fund."<sup>7/</sup> As of December 31, 1978 FMDI had outstanding 8,753,000 shares and a net asset value of \$8,166,344. In a reorganization in November 1979, similar to that of FMA, substantially all of the assets of FMDI were exchanged for shares of Oppenheimer Monetary Bridge Inc.<sup>8/</sup>

Violations of Anti-Fraud Provisions of the Securities Act, the Exchange Act, and the Advisers Act

Mound and FMAC are charged with violating and aiding and abetting violations of the anti-fraud provisions of the Securities Act, the Exchange Act, and the Advisers Act. To determine whether such charges are supported by the record necessitates an analysis of the manner in which the respondents comported themselves with respect to the funds and its shareholders in the light of respondents' duties and responsibilities toward the funds and its shareholders. As noted above, Mound was the majority stockholder and chief executive officer of FMAC, which acted as invest-

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<sup>7/</sup> Though the term "money market fund" is not defined in any statutes or Commission rules thereunder, they are generally considered to be those open-end investment companies whose portfolios consist primarily of short-term debt obligations, usually referred to as "money market instruments" (typically U.S. Treasury bills and notes, certificates of deposit, bankers' acceptances and commercial paper). These funds generally strive to maintain a constant net asset value per share. See Securities Act Release No. 6183 n. 1 (January 28, 1980), 19 SEC Docket 412.

<sup>8/</sup> On November 18, 1982 the Commission issued an order pursuant to Section 8(f) of the 1940 Act declaring that FMDI ceased to be an investment company as defined in the Act (Investment Company Act Release No. 12829; 26 SEC Docket 1111)

ment adviser to the funds, and was the chief executive officer and a director of each of the funds. The alleged violations which deal with respondents' activities and conduct vis-à-vis the operations of FMDI emanate from a policy adopted by the fund to value the instruments in its portfolio at cost plus accrued interest earned plus or minus any premium or discount, a method known (and hereafter referred to) as "the amortized cost method of valuation." In connection with the valuation method adopted by FMDI the respondents are also charged with disseminating misleading statements regarding the amortized cost method of valuation and failing adequately, to disclose the effects of the valuation policy upon shareholders.

Alleged violation by respondents of the anti-fraud provisions of the securities acts also relate to the manner in which respondents carried out their duties and responsibilities toward the shareholders of FMA. Such charges stem from investment strategy which FMAC, by and through Mound, adopted and which FMA followed in effecting purchases and sales for its portfolio. These transactions allegedly resulted in excessive portfolio turnover or "churning" of FMA's portfolio which benefitted FMAC and Mound to the detriment of FMA shareholders. In addition, FMAC and Mound are also charged with failing adequately to disclose, to shareholders and prospective purchasers of its securities, material information regarding the churning of FMA's portfolio and the consequences thereof to shareholders. The significance of the activities and conduct of the respondents upon the operations of each of the funds

and the effect of such conduct upon shareholders of the funds are discussed below.

The Conduct of Respondents Regarding The Method  
of Valuation of FMDI Portfolio

Mound was instrumental in forming FMDI in the summer of 1974. He presented to the board of directors of FMA the idea of forming a fund which would return "a much higher yield" to shareholders and recommended that FMDI would be the appropriate vehicle for such purpose. He invited the members of the FMA Board to become members of the board of FMDI. They accepted the idea and became members of the board of FMDI. From its inception in 1974 FMDI announced that its investment policy and objective was to obtain "the unusually high interest rates available on prime quality short-term obligations." This policy was stated in initial FMDI's prospectus dated August 19, 1974. In a letter on the stationary of Mound, as President, he informed prospective investors that the fund invested "solely in Short-Term (30-90 days) MONEY MARKET obligations." During the first year of its operations FMDI generally abided by its stated investment policy and acquired for its portfolio certificates of deposit and other debt instruments with maturity dates of less than one year. In April 1975 FMDI stated in its prospectus it intended to obtain "the high interest rates and liquidity available on prime quality short-term Money Market obligations."

On December 16, 1974, shortly after FMDI was organized, Mound



and the Board of Directors of FMDI adopted a resolution to value short-term certificates of deposit, bankers' acceptances and similar cash equivalents in the fund's portfolio at cost plus accrued income. A number of the members of the Board testified that in December 1974 and during 1975 they understood that short-term obligations which were valued at cost plus accrued income related to instruments with maturity dates not exceeding one year. In May 1975 Mound and the Board of FMDI considered a release issued by the Commission regarding the standardization of procedures for valuation of short-term debt instruments<sup>9/</sup> and after a discussion adopted a resolution reaffirming the method of valuing its portfolio securities which it had adopted in December 1974 to wit, that the "Fund's portfolio shall be valued at cost plus accrued income."

In 1976 Mound in an effort to obtain a higher yield for FMDI began to invest in certificates of deposit and government securities with maturities exceeding one year ("long-term instruments") and

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<sup>9/</sup> On April 15, 1975 the Commission issued Release No. 8757 under the 1940 Act to inform the public of a position it proposed to take regarding procedures for valuation of short term debit instruments owned by registered investment companies, including "money market" funds. The Commission stated that short term debt instruments include Treasury bills, securities issued or guaranteed by the U.S. Government, repurchase agreements for government securities, certificates of deposit, letters of credit, commercial paper and bankers' acceptances. The Commission, after discussing valuing such securities by "marking to market", that is, obtaining a "quote" on the particular instrument or one of comparable quality from the issuer or dealer or the use of the amortized cost valuation technique, concluded that the amortized cost appears a less desirable method of valuation because its mechanical approach, may, in many instances fail to approximate value and that "marking to market" would be more appropriate under the circumstances.

continued with this practice in 1977.

At a meeting in March 1977 Mound reported to the Board regarding the updated prospectus and a discussion was had concerning the Fund's 1976 yield and its "ability to benefit from higher yields paid on CD's with maturities of more than one year." Mound and the Board "reviewed and discussed" the current portfolio and the board concurred with Mound's plan to invest in CD's with maturity exceeding one year. A similar review of the portfolio was made at the May 1977 meeting.<sup>10/</sup>

On May 31, 1977 the Commission issued an interpretative release (#9786 under the 1940 Act) in which it stated, in essence, it would prospectively consider it inconsistent with the provisions of Rule 2a-4<sup>11/</sup> for a money market fund to use the amortized cost method of valuation to determine the fair value of debt securities which mature at a date more than 60 days subsequent to the valuation date. At a meeting of the FMDI board in June 1977 Mound reported to the board on Commission's release No. 9786 and copies were distributed to the directors. The minutes of the meeting reflect

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<sup>10/</sup> The minutes of the meeting reflect that the March meeting lasted one hour, the May meeting lasted thirty minutes.

<sup>11/</sup> Rule 2a-4, as pertinent here, provides that in calculating net asset value for the purpose of computing the price at which redeemable securities are sold or redeemed: "(1) Portfolio Securities with respect to which market quotations are readily available shall be valued at current market value and other securities and assets shall be valued at fair value as determined in good faith by the board of directors of the registered company."

that "after extensive discussion" a resolution was adopted which stated, in substance, that "it is in the best interests' of our depositors' (sic) to continue our policy..." of using the amortized cost method of valuation, authorized "management and counsel" to urge SEC not to take any action which would "require us to abandon or modify our policy" and to report back to the board. The board again "reviewed and discussed" the current portfolio<sup>12/</sup>. The Commission subsequently informed the Fund's counsel it determined not to modify its views.

In the first half of 1977 Mound continued the policy of investing in certificates of deposit, bankers acceptances and government obligations with maturities principally in excess of 60 days. Thus, the record shows that as of June 30, 1977 of total net assets of \$11,644,740 only three instruments in FMDI's portfolio, constituting less than 7% of such assets, had remaining maturities of less than 60 days and nine instruments, constituting more than 60% of net assets, had remaining maturities exceeding one year. Two of such nine instruments had maturity dates in excess of two years and another two of the said nine instruments had maturity dates of approximately four years.

As of September 30, 1977, FMDI's portfolio contained \$5,150,000 in certificates of deposit which did not mature until September 1979

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<sup>12/</sup> The minutes reflect that the entire meeting lasted one hour. Those minutes also reflect that other matters were also "discussed." For example "The Chairman (Mound) had a 'discussion' covering new depositors (sic) and increasing balances in existing accounts."

or a later date and \$700,000 in "Fannie May" obligations which did not mature until 1984.

At the next meeting of the FMDI board in October 1977 (following the June meeting) Mound reported to the Board on SEC "Interpretive Release 1C-9786" and "Marking to Market." The minutes reflect that "after extensive discussion" the board authorized management and counsel to file an action for Declaratory judgment on "Marking to Market."<sup>13/</sup> That meeting lasted one hour and fifteen minutes.<sup>14/</sup> Notwithstanding that in 1976 Mound reported to the FMDI Board that he had changed his investment strategy and intended to invest in long-term instruments, he did not recommend to the board that it rescind or amend 1975 resolution to include long-term instruments. Mound and the Board continued to use the amortized value method in valuing the portfolio of FMDI.

The record reveals that the result of the strategy pursued by Mound in 1976 and 1977 to invest in long-term instruments to obtain higher yields, was that the average weighted maturity of the investments in FMDI's portfolio at December 31, 1976 was 444 days and at December 31, 1977 was 833 days. The same average for

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<sup>13/</sup> On October 26, 1977 FMDI filed an action for Declaratory judgment in the United States District Court for the District of Columbia. The complaint was dismissed by the District Court on January 20, 1978.

<sup>14/</sup> These minutes also reflected other "discussions" took place concerning other matter and again Mound and the directors "reviewed and discussed" the current portfolio which, as of September 30, 1977, primarily included investments with maturity dates exceeding one year. Two of such instruments had maturity dates of about 7 years and four had maturity dates of about 4 years.

December 31, 1975 was only 366 days. The significance of such strategy on the fund and its shareholders is illustrated by comparing the weighted maturity of FMDI's portfolio with portfolios of other money market funds. The Investment Company Institute (a trade association for investment companies), which represented substantially the entire money market fund industry published the average weighted maturity of money market funds belonging to the Institute. The publication revealed that the average weighted maturity of such funds at December 31, 1976 was 110 days (compared with 444 days for FMDI) and at December 31, 1977 was 76 days (compared with 833 days for FMDI).<sup>15/</sup>

The documentary evidence in the record supports the finding that interest rates which started rising in the latter part of 1966, continued rising in 1977 and rose even higher in 1978. Changes in interest rates on instruments of comparable type, quality and maturity to those of certificates of deposit have a direct influence upon the fair value of certificates of deposit. When interest rates available on comparable instruments are higher than that paid by a certificate of deposit being valued, the fair value of the certificate will be less than its face value and conversely if the interest rate on comparable instruments are lower, the fair value of a certificate will be higher than its face value.

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<sup>15/</sup> The Institute's publication reflects that 48 money market funds were included in its average weighted maturity statistics in 1976 and 50 such funds in 1977. The publication also reflected that at December 31, 1978 the average weighted maturity of 61 money market funds was 42 days.

Mound testified he was aware of the rise in interest rates in the two year period and that he was concerned with interest rise trend in 1978. Notwithstanding such concern, he informed the board that in his opinion interest rates would not continue to rise much further and no change was made by Mound or the board regarding valuation of the portfolio. Mound testified it was his and the other FMDI board members' responsibility to determine the method of valuation of the fund's portfolio instruments and that he and the board knew that an increase in interest rates generally available in the market place for comparable instruments would cause the current market value of instruments in FMDI's portfolio to decline. He and the board also were aware that such changes would affect long-term instruments more than short-term instruments. In an effort to avoid the likelihood that FMDI would have to reflect a downward fluctuation in its net asset value the fund, FMDI early in 1978 effected a 10 to 1 stock split thereby reducing its net asset value from \$10 to \$1 per share. During the first half of 1978 other funds began to offer higher yields than FMDI, which was locked into long-term lower yields. As a result FMDI began, early in 1978, to suffer net redemptions, which by June amounted to \$600,000. At its board meeting in June 1978 Mound reported that interest rates continued to escalate and the possible steps to be taken to keep the fund's yield competitive. Mound led a discussion concerning the "strategy in connection with the portfolio." The minutes of the board meeting state "after discussion" the board adopted a resolution to approve "borrowing from Banks to cover redemptions."

The record discloses that the reason for borrowing rather than sell a portfolio instrument at a loss was that a sale of such instrument would, in all probability, cause FMDI's net asset value per share to decline and, as one of the board members testified, this would "cause a flood of redemptions" or as another testified they "did not want a run on the bank."

The documentary evidence reveals that during the period from August 7, 1978 to December 4, 1978 the maximum amount borrowed by FMDI at any one time was \$1,199,300. The average borrowing during the period was approximately \$523,000. Such loans were made at interest rates that averaged about 10.04% during the period. The average amount of interest the fund paid on its bank loans during 1978 exceeded the rate of returns on the highest paying instrument in its portfolio by more than 2%. Since the interest paid on the loan was an expense of the fund, the yield paid to investors in the fund was reduced. The documentary evidence in the record reflects that for the six months ended June 30, 1978, FMDI stated in its semi-annual report that its current asset value was \$11,940,384 which figure overstated the fair value of its assets by at least 1.4%. At its September board meeting, Mound discussed with the other directors the decline in the fund's assets which by that time had reached 10% and discussed the fund's ability to meet further redemptions. For the nine months ended September 30, 1978 FMDI reported it valued its portfolio instruments at \$11,450,000, a figure which the documentary evidence reveals overstated the fair value of such instruments by at least 2.6% and as much

as 4.5%. To meet the mounting redemptions Mound and FMAC determined to sell a certificate of deposit. On October 4, 1981 FMDI sold a certificate of deposit with Chase Manhattan Bank, due to mature on July 1, 1980 at a loss of approximately \$30,000 or 3% of the principal amount. At a meeting on October 17, 1978 Mound reported to the FMDI board that he sold the above mentioned \$1,000,000 certificate of deposit at a loss of \$30,000, and that the impact of this loss upon the funds shareholders was that the net asset value per share was reduced to \$.9975 based upon the amortized cost method of valuation, a figure which was "rounded to \$1.00." The effect of continuing to use the amortized cost value method at a time Mound and the board knew, or certainly must have at least realized, that it overstated the current market value of the instruments in the portfolio, was that new investors in FMDI paid "too much" for their shares, while shareholders who redeemed their shares during 1978 received more than their proportioned interest in the fund's portfolio.

There was no meeting of the FMDI board in November 1978. On December 7 and 16, 1978 the vice-president of FMAC prepared studies of FMDI's net asset value per share. The studies revealed that based upon the current market value of the instruments in its portfolio, at those dates, FMDI's net asset value was \$.94 per share.<sup>16/</sup> On December 19, Mound advised the FMDI board of FMAC's

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<sup>16/</sup> Though the record does not disclose why such studies were made by FMAC nor who requested they be prepared, it is reasonable to assume that Mound, who knew the banks had advised they would no longer continue to loan money to FMDI to meet mounting redemptions, instructed FMAC's vice-president to make the studies so the board could consider the impact of liquidation of the fund's portfolio upon shareholders which he intended to recommend to the board.



intention to liquidate the fund's portfolio and that such liquidation would reduce FMDI's net asset value from \$1.00 to approximately \$.94 per share. On December 20, 1981 FMAC liquidated the entire portfolio of FMDI and reinvested the proceeds in short-term instruments. As a result of the liquidation FMDI sustained a loss of \$509,151 and FMDI's per share net asset value was reduced to \$.94 per share.

The record sustains a finding that Mound, chief executive officer and director of FMDI and FMAC determined from the inception of FMDI that the portfolio of the fund be valued by using the amortized cost method of valuation.<sup>17/</sup> Since FMDI, as noted, was a registered open-end management company it constantly offered to sell redeemable shares of the fund to the public.<sup>18/</sup> Because such shares represent a proportionate interest in the underlying assets of the fund, the sale of such shares at too low a price or the redemption of such shares at too high a price, the proportionate interests of other shareholders in the fund's assets are diluted. Hence, it is essential that when such shares are sold or redeemed they be priced properly so as to reflect the value of the shareholders proportionate interest in the fund's assets. In an effort to make certain

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<sup>17/</sup> The record reflects that FMDI adopted the amortized cost method of valuation in December 1974 by resolution which authorized "Management not mark to market."

<sup>18/</sup> A "redeemable security" is defined in Section 2(a)(32) of the 1940 Act as any security which entitles the holder to receive approximately his proportionate share of the issuer's current net assets, or the cash equivalent thereof.

that redeemable securities are priced in a fair and equitable manner the Commission, pursuant to authority granted to it in Section 22(c) of the 1940 Act, adopted Rule 22(c)(1) which, in general, provides that open-end companies may not sell their shares at a price other than one based upon their net asset value. The term "value" is defined in Section 2(a)(41) of the 1940 Act. It is defined in pertinent part as:

"(i) with respect to securities for which market quotations are readily available, the market value of such securities; and (ii) with respect to other securities and assets fair value as determined in good faith by the board of directors . . . "

This definition is also used in Rule 2a-4 under the 1940 Act as the required basis for computing periodically the current net asset value of redeemable securities of investment companies for the purpose of pricing their shares. (Fn11 supra)

On at least three occasions since 1969 the Commission has interpreted "fair value" for securities for which market quotations are not readily available to mean the price that would be received upon the current sale of security or asset.<sup>19/</sup> In December 1970 the Commission published a release in which it stated its view regarding

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<sup>19/</sup> In 1969 the Commission issued a release covering problems relating to so-called "restricted securities" in portfolios of investment companies and stated: "As a general principle, the current fair value of restricted securities would appear to be the amount which the owner might reasonably expect to receive for them upon their current sale." Investment Company Act Release No. 5847 (October 21, 1969)

the manner of determining "fair value" and the persons primarily responsible for determining the method of arriving at fair value. With respect to "fair value" the Commission said:

"No single standard for determining "fair value . . . in good faith" can be laid down, since fair value depends upon the circumstances of each individual case. As a general principle, the current "fair value" of an issue of securities being valued by the Board of Directors would appear to be the amount which the owner might reasonably expect to receive for them upon their current sale. (emphasis supplied) (Investment Company Act Release No. 6295, December 23, 1970).

With respect to the persons responsible for determining the method of arriving at fair value the Commission in that 1970 release specifically pointed out:

"To comply with Section 2(a)(30)(now numbered 41) of the Act and Rule 2a-4 under the Act, it is incumbent upon the Board of Directors to satisfy themselves that all appropriate factors relevant to the value of securities for which market quotations are not readily available have been considered and to determine the method of arriving at the fair value of each such security. To the extent considered necessary, the board may appoint persons to assist them in the determination of such value, and to make the actual calculations pursuant to the board's direction. The board must also, consistent with this responsibility, continuously review the appropriateness of the method used in valuing each issue of security in the company's portfolio. The directors must recognize their responsibilities in this matter and whenever technical assistance is requested from individuals who are not directors, the findings of such individuals must be carefully reviewed by the directors in order to satisfy themselves that the resulting valuations are fair." (Investment Company Act Release 6295)

In April 1975 the Commission published a release to inform the public of a position it proposed to take regarding standardization of procedures for valuation of short-term debt instruments owned by registered investment companies, including "money-market in-  
funds.<sup>20/</sup> The release states that the Commission believes it would

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<sup>20/</sup> The release notes that some of the money-market funds value their short-term instruments on an amortized cost basis and that such instruments include treasury bills, securities issued or guaranteed by the U.S. Government, repurchase agreements for government securities, Certificates of deposit, letters of credit, commercial paper and banker's acceptances. (emphasis supplied)

be desirable to discontinue the amortized cost method of valuation and points out among the reasons for its belief was that such method fails to reflect the impact of fluctuation in prevailing interest rates upon the market value of the portfolio instruments. Such method of valuation, the release notes, may result in periods during which the value of a fund's portfolio, as determined by amortized cost, is significantly higher or lower than the price the fund would receive if it liquidated the portfolio at prevailing market prices. Shareholders would thus be exposed to risk of unfair dilution. Investment Company Act Release No. 8757 (April 15, 1975). At a meeting of the FMDI board of directors in April 1975 Mound lead a discussion of the aforesaid release with the fund's board and he and the board determined to continue using the amortized cost method of evaluation.

When the Commission published Release No 9786 under the 1940 Act in May 1977<sup>21/</sup> it painstakingly called attention to the duty and responsibility of a board of directors to value securities with maturities longer than 60 days, where market quotations are not readily available, in such a manner as to take into account any unrealized appreciation or depreciation due to changes in interest rates and other factors which would influence the current fair value of such securities. It specifically declared that the use

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21/ As noted earlier this release stated the Commission would prospectively consider it inconsistent with the provisions of Rule 2a-4 for a money market fund to use the amortized cost method of valuation to determine fair value of debt securities maturing more than 60 days after the valuation date.

of the amortized cost method to value securities with longer maturities:

". . . . cannot in the future represent a 'good faith' effort to determine the fair value of portfolio securities for purposes of Rule 2a-4; such valuation fails to consider the impact of market factors subsequent to the date a debt security is purchased on the value of such security. Moreover, the probability that amortized cost valuations will not approximate fair value is progressively greater for securities of increasingly longer maturities.

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Boards of directors of money market funds . . . . should consider and re-evaluate current fund pricing practices in light of the positions expressed herein."  
(emphasis supplied)

Notwithstanding that by May 1977 Mound had changed the investment strategy of FMDI by concentrating almost exclusively in long term certificates of deposit, he merely reported to the Board on "Release 1C-9786" but there is no evidence in the record that he recommended that the board accept the Commission's request that boards "should re-evaluate current fund pricing practices." Mound and the FMDI board, after discussing the release, decided again to continue to use the amortized cost method of evaluation. Upon the basis of the foregoing, it is concluded that the persistence of Mound and the board to continue to follow the practice of using the amortized cost method of valuation during 1977 and particularly in 1978, when interest rates were continuing to rise, constituted a lack of a "good faith" effort to determine "fair value" for purposes of Rule 2a-4. The record amply demonstrates that Mound and the board obstinately refused to recognize the impact of rising interest rates, or other market factors subsequent to the date of the FMDI portfolio secur-

ities were purchased, on the value of such securities. The valuation practices by Mound, FMAC, the investment adviser to the fund, and the board of directors also constitutes a breach of the duties and responsibilities which they owe to shareholders of the fund to properly value the fund's portfolio.

Mound, as chief executor officer and director fo FMDI and FMAC's chief officer, and FMAC as investment adviser to the fund were fiduciaries with respect to the fund and its shareholders. Consumer-Investor Planning Corp., et al 43 SEC 1096, 1100 Fm 7 (February 20, 1969); Brown v. Bullock 194 F Supp 207, 229 (SDNY 1961), aff'd 294 F.2d 415(C.A. 2, 1961). As such they were under a duty to act solely in the best interests of the fund and its shareholders. Winfield & Co. Inc. 44 SEC 810,814 (February 9, 1972). This, the record establishes, Mound and FMAC did not do. As early as 1969 when it published Release 5847 under the 1940 Act (referred to earlier) regarding restricted securities, the Commission pointed out that improper valuation of restricted securities held by a management investment company would distort the net asset value of the shares such company offered or redeemed and would constitute a fraud and deceit within the meaning of the anti-fraud provisions of the Exchange Act. The Commission succinctly stated:

"The offering price of securities issued by a management investment company is premised upon net asset value of such shares as determined pursuant to Section 2(a)(39) (now 2(a)(41)) of the Act and Rule 2a-4 thereunder and is so represented in its prospectus. the improper valuation of restricted securities held by such a company would distort the net asset value of the shares being offered or, in the case of an open-end company, redeemed, and would therefore constitute a fraud and deceit within the meaning of Section 10(b) and Rule 10b-5." (emphasis supplied)

The Commission since the publication of the foregoing, has consistently held that improper violation practices violate the anti-fraud sections of the Federal securities laws and that officers and directors of the investment company and the investment adviser to the fund who were responsible for the improper valuation practices violated the anti-fraud provisions of the Securities Act, the Exchange Act and the 1940 Act. In 1970 the Commission, in Mates Financial Services 44 SEC 246 found that the proprietor of an investment adviser, who was also an officer and director of the investment company managed by the adviser, wilfully violated and aided and abetted violations of Section 206(1) and (2) of the Advisers Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder by causing the investment company to improperly value its portfolio securities. In 1972 the Commission again found that an investment adviser and its officers had fiduciary obligations to the investment company and its shareholders and that when they caused the directors of the fund to use improper valuation practices, wilfully violated the anti-fraud provisions of the Securities Act, the Exchange Act and the Advisers Act, Winfield & Co. Inc. supra. Similarly in 1975 the Commission held that the continuing over-evaluation of the fund's net asset value was fraudulent and the president and director of an off-shore mutual fund who caused the fund to overvalue its assets thus inflating its net asset value wilfully violated and aided and abetted violations of the anti-fraud provisions of the Securities Act, the Exchange Act and the Advisers Act Robert F. Lynch 8 SEC Docket 75 (October 15, 1975).

Mound in an effort to justify his and FMAC's conduct testified he considered it was too expensive and too burdensome to "mark to market", that the CDs which were in the FMDI portfolio were not readily marketable, that since he intended to hold the portfolio securities to maturity the use of the amortized cost method of valuation was proper, that in 1977 and the first half of 1978 he did not believe interest rates would continue to rise and that from 1975 he made no effort to ascertain from any broker or any other source what the sale value was of the portfolio securities. He also testified he knew that if he wanted to sell portfolio securities the fund would "have to take a loss on everything we had" but since he had "no vision of ever having to sell, it would have been an exercise in stupidity, to have marked something on the basis which we did not expect to happen . . . and we never expected that a situation would arise where we would be compelled to give up our plan, which always was to hold things to maturity. . . and then a catastrophe happened." The catastrophe which Mound referred to in his testimony was the necessity to sell a portfolio security in October 1978 at a 3% loss to meet mounting redemptions and ultimately the sale of the entire portfolio in December 1978 with the result that shareholders who remained in FMDI until such liquidations were forced to absorb the entire 6% loss. None of Mound's explanations are sufficient to exculpate Mound or FMAC from their fiduciary obligation to FMDI and its shareholders to properly value the portfolio securities particularly since they were on notice since 1975, and of utmost significance since 1977 when the Commission published Release



No. 9786 that the practice of using the amortized cost method of valuation without giving adequate consideration of the impact of the continuing rising interest rates could result in significantly higher or lower prices than the price the fund would receive if it liquidated the portfolio at prevailing market prices. In fact, as noted above, Mound made no attempt from 1975 to ever attempt to ascertain the prevailing market price of any portfolio security.

It is concluded that the conduct of Mound and FMAC, as fiduciaries of FMDI in so far as they approved and continued to permit the use of the amortized cost method of valuation of the portfolio securities of FMDI as detailed above, was a breach of their fiduciary responsibilities to FMDI and its shareholder and they thereby engaged in acts, practices and courses of business which operated as a fraud and deceit upon shareholders of FMDI. Mound and FMAC are found to have wilfully violated and wilfully aided and abetted violations of the anti-fraud provisions of the Securities Act, the Exchange Act and the Advisers Act, as charged in the Order.

The Violative Conduct of Respondents Regarding Alleged Failure Adequately to Disclose Material Information Relating to the Operations of FMDI

Respondents Mound and FMAC are also charged with violating the anti-fraud provisions of the Securities Act, the Exchange Act and the Advisers Act by making untrue statements of material facts and omitting to state material facts with respect to the operations of FMDI. Specifically the Order alleges that Mound and the other director respondents caused FMDI to file with the Commission and/or

disseminate to shareholders and prospective shareholders annual and quarterly reports, prospectuses, and selling materials which misrepresented or failed to disclose material facts concerning FMDI's pricing practices, the value of its portfolio securities, its capital losses, the liquidation of substantially its entire portfolio at a capital loss and the resulting reduction in the net asset value of a share of FMDI from \$1 to \$.94.

Commencing with its initial prospectus dated September 24, 1974 FMDI boldly featured on its cover page that it offered "Minimum Safety of Capital" and stated under the caption "Investment Policy and Objective" that it intends "to serve its depositors (sic) by obtaining for them the unusually high interest rates available on prime quality short-term obligations by acquiring them as shares of mutual funds which invest in them." The prospectus also stated that pursuant to an agreement FMAC, as the funds investment manager "shall select, supervise and manage the Fund's investments." In a letter in 1974 signed by Mound as President of FMDI<sup>22/</sup> he informed prospective investors "we invest solely in Short-Term (30-90 days) MONEY MARKET obligations ...." The next prospectus dated April 2, 1975 again featured boldly on its cover page that it offered "Maximum Safety" and that stated FMDI intended to obtain "the high interest rates and liquidity available on prime quality Short-term Money Market obligations" but deleted the reference to other funds. The 1974 or 1975 prospectuses omitted to disclose the material fact that there was an inherent risk that a rise in interest rates might cause the value of a shareholder's

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<sup>22/</sup> Though the letter is undated it was received by the Commission October 21, 1974.

investment to decline.

The documentary evidence discloses that in 1976 FMAC, as Manager of FMDI's assets, and Mound, its president, in an effort to obtain higher yields began investing FMDI's funds in certificates of deposit and government securities with maturity terms exceeding one year (long-term instruments). Thus, as at December 31, 1976 FMDI's total assets was \$7,673,185 of which about \$4,503,271 or about 60% was invested in certificates of deposit with maturities in 1978 (in excess of one year) and a total investment in government securities about \$519,650 or about 6.5%, with securities in 1978 ( in excess of one year).

The same policy of investing in long-term instruments was followed in 1977. As of September 30, 1977 approximately \$700,000 of FMDI's portfolio consisted of Fannie Mae obligations maturing in 1984 and \$5,150,000 in certificates of deposit maturing in 1979 or later. The total of these investments was in excess 50% of FMDI's portfolio as of the aforementioned date. Though the 1975 prospectus asserted that FMDI invested "Solely in" short-term obligations the succeeding prospectuses failed to disclose the material information that FMDI had changed its investment policy by investing in long-term certificates of deposit, nor did they disclose that its stated investment policy of "high yield and safety" exposed shareholders of the risk that the value of its long-term investments might decline if interest rates rose. In addition, the prospectuses used by FMDI in 1976 and 1977 described in a footnote to the financial statements that "certificates of deposit and other short-term instruments are carried at cost

plus accrued interest which approximates market value" was false, or at the very least misleading, to the extent it stated instruments are carried at a value which approximates market value. The record amply demonstrates that neither Mound<sup>23/</sup> nor the funds directors made any effort in those years to ascertain the market value of long-term certificates of deposit. Though the 1978 prospectus for the first time included a separate section entitled "HOW NEW ASSET VALUE IS DETERMINED" purported to describe how FMDI determined its net asset value for purposes of sale and redemption<sup>24/</sup> it too was false to the extent it claimed a "new asset value" was being determined when in fact the method used was the same as in previous years and false to the extent it professed that the board of directors made a "good faith" effort to determine fair value of its certificates of deposit when in fact, Mound and the other directors individually or collectively as a board, made no effort whatsoever from 1975 to about December 1978, to obtain a market value for such certificates of deposit.

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23/ See reference to Mound's testimony P 22 supra

24/ The 1978 prospectus represented:  
"HOW NEW ASSET VALUE IS DETERMINED"  
The Fund intends to maintain its shares at a constant net and value of \$1.00 per share. The net asset value per share (for the purpose of calculating the price at which shares are issued and redeemed) is determined by:  
(a) valuing securities for which market quotations are readily available at the market value and other securities and assets at Fair Value as determined in good faith by the Board of directors, (b) deducting the Funds liabilities, (c) dividing the resulting amount by the number of shares outstanding and (d) adjusting to the nearest full cent ...."

The record further reveals that Mound and the directors failed to disclose to shareholders that FMDI had made loans in 1978 to raise cash in order to meet redemptions, nor did they disclose the effect which such loans had upon the fund's yield. After Mound sold a portfolio security for the fund at a loss of 3% he failed to disclose to the stockholders appropriate information regarding such loss and failed to amend FMDI's 1978 prospectus with respect to its statement that the fund intended to hold all instruments to maturity. Mound testified that despite the fact he knew the fund was experiencing net redemptions and that the fund's prospectus stated it intended to hold its instruments to maturity, he did not consider it necessary to amend the prospectus to reflect the material information regarding the sale of a portfolio security to meet redemptions.

The information relating to changes in the investment policies of the fund, the amortized cost method used by Mound and the other directors of the fund to calculate the fund's net asset value, the information relating to the factors involved in the investment strategy employed by Mound which exposed shareholders to risk that the value of their investment might decline if interest rates rose is important to a shareholder who is determining to invest or retain his investment. Proper calculation of the valuation of portfolio securities by a money market fund is of critical importance since it largely determines the price at which securities are sold or redeemed. Investors may be misled by the reported performance of an investment company where portfolio securities are not properly valued. Moreover, the failure to disclose information that the fund

borrowed money to meet redemptions together with the effect of such loans upon the fund's yield is the type of information which is material to a shareholder considering whether to invest or retain his investment in the fund. The Supreme Court has held that the question of materiality "is an objective one involving the significance of an omitted or misrepresented fact to a reasonable investor . . . . Put another way, there must be a substantial likelihood that disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the "total mix" of the information made available." TSC Industries v. Northway Inc. 426 U.S. 438, 444 (1976). The false or misleading information concerning the matters noted above and the failure to disclose material information concerning the fund's operations was of sufficient moment to create a substantial likelihood that a shareholder of FMDI would consider it of significant importance in making his decision. Adequate disclosure of all of the above mentioned matters is essential in order to give investors the means of understanding the intricacies of the operations into which they are invited and to enable investors to appraise the true nature of the fund's operations. Mound was under a duty to bring "the complex of circumstances . . . to [the investor's] attention lucidly and forcefully."<sup>25/</sup> This he failed to do. It is concluded that Mound wilfully violated and wilfully aided and abetted violations of the anti-fraud provisions of the Securities Act, the Exchange Act and the Advisers Act by making untrue statements of material facts and omitting to state material facts necessary to make the statements made, in light of the circumstances under which they were made not misleading.

The charges that FMAC made misrepresentations and omitted to state material facts in wilful violation of the foregoing anti-fraud provisions of the securities acts are not supported by the record and are dismissed. Though the agreement between FMDI and FMAC required the latter entity to manage and supervise the fund's investments, it is silent with respect to the function of preparation of prospectuses. Mound testified, and his testimony at least in this area is unrefuted, that FMAC under its agreement was required only to supervise and manage the fund's portfolio but it had no responsibility to prepare any of the prospectuses. He also testified they were prepared by counsel for FMDI who sent them to him and to the other directors for signature and that his review of the prospectuses was in his capacity as chief executive officer of the fund. In addition, the dissemination of the prospectuses was the responsibility of the fund and not FMAC. The record thus is insufficient to establish that FMAC, as such, had any duty or responsibility with respect to the contents of the prospectuses or that it, in fact, prepared any of them.<sup>26/</sup>

Conduct of Respondents With Respect to FMA

As noted earlier respondents are charged with violating and aiding and abetting violations the anti-fraud provisions

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<sup>26/</sup> It is noted that the Division's proposed findings and conclusions contends that only Mound (and the directors) misrepresented or omitted to state material facts in violation of the anti-fraud provisions mentioned above.

of the securities laws in that they employed devices, schemes and artifices to defraud and engage in acts, practices and courses of business which acted as a fraud and deceit upon purchasers and prospective purchasers of FMA securities and made untrue statements of material fact and omitted to state material facts. Respondent's conduct which formed the basis of the charges is that they caused FMA to engage in excessive portfolio transactions which resulted in the enrichment of FMAC and Mound, at the expense and to the detriment of FMA and its shareholders and misrepresented or failed to disclose material information regarding FMA's portfolio transactions.

FMA, since its inception until 1979, was a "fund of funds" which invested substantially all of its assets in shares of other investment companies. Pursuant to a management agreement FMAC selected, supervised and managed the investments of FMA's assets. FMAC also acted as principal broker for FMA in purchasing shares of load funds for its portfolio. As broker FMAC earned and retained commissions paid by the underwriters of load funds in which FMA invested. FMA's investment objective as stated in its prospectuses from 1974 through 1978 was "long term growth". To achieve this objective FMAC and Mound adopted an investment strategy for FMA pursuant to which it bought and sold shares of other investment companies on the basis of "noting" their performance over the preceeding four to thirteen weeks. Mound testified " . . . we never examine their [the funds in which FMA invested] portfolio holdings. We were not capable . . ." and that he and FMAC made no attempt to examine the port-



folio holdings of the funds in which FMA invested. Their sole concern was performance and if Mound or FMAC believed a fund in which it invested FMA's assets did not, in the four to thirteen week period, perform as expected, Mound switched into either another series of the same fund or to another fund which he felt would perform better.

The record clearly establishes that FMAC under its management contract with FMA had the responsibility to select, supervise and manage FMA's assets. In accordance with such responsibility FMAC and Mound, its chief executive officer, selected the particular investment company whose shares FMA would purchase and sell. All decisions concerning when purchases and sales were to be consummated for FMA's portfolio were made by Mound and FMAC. From at least 1975 through 1978, FMA's prospectuses, disclosed that FMAC acted as FMA's principal broker in buying shares of load funds for the latter's portfolio and that in acting as broker earned and retained commissions paid by underwriters of load funds in which FMA invested.

The record reveals that the strategy adopted by Mound and FMAC in selecting and managing the portfolio of FMA resulted in a turnover of FMA's portfolio which, over the four year period between 1975 and 1979, exceeded every other fund in the industry.<sup>27/</sup>

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<sup>27/</sup> Portfolio turnover rate of a mutual fund is a measure of the activity of the portfolio and the frequency of purchases and sales, in relation to the net asset value of the fund. The turnover rate is calculated by dividing the lesser of the purchases and sales over the average net asset value of the fund, for the year.

The excessive rate of turnover of the FMA portfolio for the years 1975 through 1978 is best demonstrated by comparing FMA's portfolio turnover rate with that of other investment companies. Table 1 below shows the portfolio rates of investment companies as compares with FMA's portfolio turnover rate.

TABLE 1

FMA Portfolio Turnover Rate  
 Compared to Portfolio Turnover Rates of  
 Companies Listed in the Lipper Analytical Distribution<sup>28/</sup>  
 1975 - 1978

Portfolio Turnover Rate (Percent)	Percentage of all Investment Companies listed in the Lipper Analytical Distributions having indicated Portfolio Turnover Rates			
	1975	1976	1977	1978
	0 - 50	60.7%	60.0%	70.9%
51 - 100	28.6	28.3	23.7	26.2
101 - 175	7.9	10.3	4.3	7.5
176 - 250	1.8	.8	1.1	1.6
251 +	1.0	.6	.7	1.1
<u>FMA Portfolio Turnover Rate</u>	<u>480%</u>	<u>389%</u>	<u>498%</u>	<u>455%</u>

An analysis of the data in the above table reveals that FMA's turnover rate of 480% for 1975 was higher than at least 99% of all investment companies registered in the United States: that its rate of 389% for 1976 was higher than that of at least 99.4% of all registered investment companies; that its rate of 498% for 1977 was higher than that of at least 99.3% of all registered investment companies and its turnover rate of 455% for 1978 was higher than that of at least 89.9% of all investment

<sup>28/</sup> The record discloses that the rates shown in the Table related to about 500 investment companies and was compiled from data published by Lipper Analytical Distributors Inc, commonly referred to in the industry as the Lipper Service. The record also shows that Mound and FMAC used the "Lipper Reports" in connection with their selection and management of the FMA portfolio.

companies. The investment strategy adopted by Mound and FMAC resulted in a portfolio turnover rate for the years 1975 through 1978 which, as noted, exceeded every other fund in the industry. The Commission has held that turnover rates ranging from 44% to 97% are "unusually high for a mutual fund" Managed Funds Inc., 39 SEC 313,323 (1969). Portfolio turnover rates between 389% and 498% over a four year evinces a pattern of engaging in excessive trading, particularly in light of FMA's stated objective of long-term growth which Mound attempted to achieve by investing in funds based on a four to thirteen week performance. The detrimental effect of FMA's excessive portfolio trading upon shareholders of the fund is illustrated by a retroactive analysis of such trading in each of three successive years beginning January 1, 1976. The record reveals that if FMA had held its portfolio of January 1, 1976 through December 31, 1978, without engaging in any portfolio purchases or sales during the said period, its net asset value per share would have been \$1.78 higher than it actually was at December 31, 1978. Similarly, if FMA had held its portfolio of January 1, 1977, without making any trades over the next two years, its net asset value per share would have been \$2.00 higher than it actually was at December 31, 1978. If FMA had held its portfolio of January 1, 1978, without purchasing or selling any portfolio securities during that year, its net asset values per share would have been \$.42 higher than it was at December 31, 1978. It is quite apparent that the strategy

employed by Mound and FMAC of trading FMA's portfolio securities on the basis of their short term performance failed to achieve the long term growth investment objective as represented in its prospectuses.

Another measure of the detrimental effect of FMA's excessive portfolio trading upon its shareholders is also demonstrated by comparing the performance of FMA between January 1, 1976 and December 31, 1978 with that of mutual fund industry average. The record reveals that for the aforesaid period FMA's performance failed to match the mutual fund industry average. If FMA had kept pace with the industry average its net asset values would have been \$1.01 higher than it actually was as at December 31, 1978.

The manner in which Mound and FMAC managed the FMA portfolio not only caused excessive portfolio turnover, as noted above, but it also generated substantial benefits to FMAC and Mound. Because FMAC acted as principal broker in purchasing shares of load funds for the FMA portfolio, FMAC received commission (dealer allowances) from the underwriters of the load funds invested in by FMA. Since 1971 FMAC has been permitted to retain commissions received from underwriters not exceeding 1% of the purchase price.<sup>29/</sup> If the commissions which FMAC received from the underwriter exceeded 1% of the purchase price, FMAC credited the excess amount to FMA as a reduction of the

management fee paid to FMAC. Though many of the FMA purchases were of shares of no load funds and imposed no cost on the fund, the magnitude of Mound's trading activity was such that FMA's commission expenses were excessive when measured as a percentage of the fund's net assets. The record reveals the following total commission received, the amount credited to FMA and the commission retained by FMAC.

	1974	1975	1976	1977
TOTAL COMMISSIONS	\$240,521	\$319,828	\$308,062	\$206,772
AMOUNT CREDITED TO FMA	57,382	37,086	47,724	36,602
COMMISSIONS RETAINED	183,139	282,742	260,338	170,170

An analysis of FMA's commissions expenses, when measured as a percentage of net assets, discloses an excessive commission ratio <sup>30/</sup> resulting from the trading activity of Mound and FMAC. The evidence reveals that FMA's commission ratio was 2.65% in 1975 and 2.05% in 1976 (based upon figures disclosed in its prospectuses) which were greater than that of 98.1% of all investment companies. In 1975 and 1976 FMA's aggregate commission expenses exceeded 2% of the fund's net assets. In 1977 FMA's commission ratio was 1.75% which was greater than that of 97% of all investment companies and in 1978 FMA's commission ratio was 1.54% which was greater than that of 98.8% of all investment companies. The analysis shows that in 1978 about 83.3% of all investment companies had a commission ratio of 1/2% or less.

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<sup>30/</sup> The commission ratio represents total commission dollars paid by a mutual fund as a percentage of its average net assets and measures the cost which portfolio turnover imposes on the fund as well as the impact of commission dollars on the fund and ultimately on the fund shareholders.

The commissions received by FMAC from its excessive trading of FMA's portfolio was the primary source of FMAC's income and that of Mound. It was at least four times greater in 1974, 1975 and 1976 and about three times greater in 1977 than the amounts FMAC received under its management agreement with FMA. The FMA prospectuses disclosed that the net management fee retained by FMAC (after crediting FMA with the excess of 1% of the purchase price of the shares bought for the FMA portfolio) amounted to \$28,578 in 1974, \$60,416 in 1975, \$58,499 in 1976 and \$71,303 in 1977. The record further reflects that absent the commission revenue which it derived from its excessive trading activity for the fund, FMAC would have been rendered insolvent.

Upon the basis of the foregoing it is concluded that Mound and FMAC caused FMA to engage in excessive trading of its portfolio securities in disregard of its stated objective and that Mound and FMAC were motivated to effect such trading for FMA with the intention and purpose of generating commissions for FMAC.

It is well settled that excessive trading or "churning" occurs when a securities broker enters into transactions and manages a clients' account for the purpose of generating commissions and in disregard of the client's interests. Miley v Oppenheimer & Co. 637 F2d 318,324 (5th Cir. 1981). To establish a claim of churning, three requisites elements must be shown; (1) that the trading in the client's account was excessive in

light of his investment objectives; (2) that the broker or investment adviser in question exercised control over the trading in the account; and (3) the broker or investment adviser acted with intent to defraud or with the wilfull and reckless disregard for the interests of his client.

Mihara v Dean Witter & Co Inc. 619 F2d 814,821 (9th Cir. 1980); Miley v Oppenheimer supra.

The record in the instant case amply supports the finding that all three elements are present. As noted earlier, the turnover rate of the FMA portfolio from 1975 through 1978 ranged from 389% to 498% was found to be excessive in light of the stated investment objective of "long-term growth". Additionally, the excessive trading was found to be detrimental to the interests of FMA's shareholders.

The second element - exercise of control over the trading - is also supported by the record by reason of the management agreement between FMAC and FMA which required FMAC to select, manage and supervise the investments of the fund. Mound unquestionably functioned primarily in selecting and managing the portfolio.

With respect to the third element the record supports the finding that FMAC and Mound utilized an investment strategy for managing and supervising the FMA portfolio which generated substantial revenue for their personal benefit and profit. The record is devoid of any evidence that Mound made any effort to determine whether the excessive trading warranted the substantial

costs. Under the circumstances Mound and FMAC are found to have acted in wilfull and reckless disregard for the interests of FMA and its shareholders, to have employed devices and artifices to defraud and engaged in acts and practices and a course of busniess which operated as a fraud or deceit upon the purchasers of prospective purchasers of FMA shares in wilfull violation of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, Section 17(a) of the Securities Act and Section 206(1) and (2) of the Advisers Act.

FMAC and Mound are also charged with violating the above provisions of the securities acts in making untrue statements of material facts and omitting to state material facts necessary to make the statements made not misleading. In essence, these charges relate to the nature of the disclosures made in the FMA prospectuses and the failure to disclose the costs which the strategy used by Mound imposed upon the fund's shareholders.

FMA's prospectuses contained only the amount of commission dollars earned by FMAC as principal broker on transactions of the fund involving the shares of load funds. The commission earned by FMAC generally ranged between 80 and 90% of the total sales load paid by FMA on such transactions. As a consequence, the total amount of commission dollars paid by FMA was approximately 15% greater than the amount reflected in the prospectus and the prospectuses thus were misleading in stating only the dollar amount earned by FMAC.

From 1975 through 1977 the prospectuses of FMA reflected FMA's commission costs as a percentage of the total purchases and sales for its portfolio and that as a result of investing in no load funds and taking advantage of switching privileges in funds under the same management, the fund's costs "has been held" to stated percentages. Each such prospectus failed to disclose that the commission expenses incurred by FMA when calculated as a percentage of its net assets were abnormally high, particularly when compared with similar expenses of other mutual funds. In fact, such costs when examined as a percentage of the net assets of the fund were the highest in the industry. The.



disclosure of aggregate commission costs on a percentage of total purchases and sales rather than as a percentage of net assets inhibited shareholders from making a considered investment judgment of FMA costs as compared with costs of other funds. In TSC Industries v Northway, supra the court held "An omitted fact is material if there is a substantial likelihood that a reasonable stockholder would consider it important in deciding how to vote".

The prospectuses used by FMA in 1975, 1976 and 1977 failed to disclose any information concerning the portfolio turnover rate of the fund. The lack of such information constitutes a failure to disclose a material fact to shareholders and prospective investors. Moreover, the prospectuses used by FMA through 1978 failed to disclose that FMAC and Mound directly benefited from the commissions derived from the fund's purchases and that FMAC depended upon such commission to remain solvent. Such information was material to shareholders to permit them to evaluate the effectiveness and objectivity of the investment decisions made by Mound, particularly since the money they entrusted to his management was being used to engage in excessive transactions which during 1975 through 1978 resulted in an unusually high turnover rate and a commission ratio exceeding the ratio of 97 to 98.8% of funds in the industry.

The record supports the finding that Mound prepared the initial prospectus of FMA and bore the responsibility for the information contained in subsequent prospectuses. Such respon-

sibility carried with it the duty to fully disclose the mode of his operations.<sup>31/</sup> The Commission has held that persons directing the execution of portfolio transactions and those acting as investment advisers are fiduciaries of the fund. As such, they were under a duty to act solely in the best interests of the fund and its shareholders. Winfield & Co Inc supra. In the instant case the record amply supports the finding that Mound was a fiduciary of the fund and under a duty to make full and adequate disclosure concerning the manner in which he was managing and supervising FMA's portfolio, that the trading he caused FMA to engage in was excessive and that as a result he benefited substantially therefrom to the detriment of the shareholders. Accordingly, it is concluded that by engaging in the conduct described above Mound wilfully violated Section 17(a) of the Securities Act, Section 10-b of the Exchange Act and Rule 10b-5 thereunder.

For the reasons stated on P 29 supra dismissing the charges that FMAC made material misrepresentations and omitted to state material facts with respect to the operations of FMDI, the charges that FMAC made material misrepresentations and omitted to state material facts with respect to the operations of FMA in wilfull violation of the above mentioned anti-fraud provisions of the securities acts are also dismissed.

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<sup>31/</sup> Mound's testimony that he did not personally prepare the subsequent prospectuses does not exculpate him from his responsibility for the information contained therein.

Wilfull Violation of Section 15(c) of the 1940 Act

Mound and FMAC are charged with violating Section 15(c) of the 1940 Act by failing to furnish such information as was necessary, in the exercise of their fiduciary obligations, to evaluate the terms of the funds' advisory contracts. Section 15(c) of the 1940 Act, as pertinent here, provides that

"it shall be . . . the duty of an investment adviser to such company[a registered investment company] to furnish such information as may reasonably be necessary to evaluate the term of any contract whereby a person undertakes regularly to serve or act as investment adviser of such company . . . . "

The record discloses that the directors of FMA and FMDI annually approved and recommended that the shareholders of each of the funds approve the management agreements between FMAC and both funds. At meetings of the boards of directors of each of the funds held on March 24, 1977 Mound and FMAC proposed that each of the boards recommend to the shareholders approval of a change in management agreements to provide that each of the funds bear its own expenses for rent and telephone and that FMA also pay clerical expenses. Each of the boards approved the proposal. At the time such amendments were submitted, the shareholders were informed (in the proxy material) that it was estimated that FMDI's annual expenses for rent and telephone would total \$11,000 and FMA's annual expenses for rent telephone and clerical help would be \$31,000.

The record supports the finding that at the time Mound and FMAC recommended to the boards of directors that the management

agreement between FMAC and the two funds be modified, they failed to furnish such information as may reasonably be necessary to evaluate the agreements. Mound and FMAC failed to furnish information concerning the amount of commission received by FMAC. No information was made available to the directors concerning the extent to which the commission revenue retained by FMAC, when considered as a percentage of FMA's total net assets, exceeded the amount retained by affiliated brokers for other investment companies. Mound testified he understood that the commission paid by FMA represented a smaller expense in percentage terms than the commission expenses incurred by investment companies generally. The record shows, as earlier noted, that FMA spent a larger portion of its net assets than at least 97% of funds in the industry.

Mound and FMAC failed to furnish information to the directors of the funds at the time the management contract was amended regarding the extent to which other companies paid the type of expenses which FMAC was requesting both the funds pay. One of the directors testified the only information he received concerning expenses which other funds paid was that it was "customary for the fund to bear such expenses and that FMAC's expenses had risen." Mound also claimed that FMAC's expenses had increased. To evaluate the term of the management contract it would be necessary or, at the very least, important to know what other companies paid by way of expenses together

with detailed information concerning the nature of the expenses which FMAC claimed had increased. Mound did not furnish such information.

Mound and FMAC failed to furnish information regarding the extent to which FMAC profited from the relationship with the two funds.

It is evident from the minutes of each of the March meetings of the boards of the directors that the proposals by Mound and FMAC to have each of the funds bear its own expenses were accepted by the directors in perfunctory fashion with no information being furnished to permit any evaluation of the management contract.

The Courts have held that under the scheme of the 1940 Act an investment adviser is "under a duty of full disclosure of information to . . . unaffiliated directors in every area where there is a possible conflict of interest between their interests and the interests of the fund" Fogel v Chestnutt 553 F.2d 731,745 (1975). In that case Judge Friendly noted that the 1940 Act's requirements carries with it the obligation of the investment adviser to insure that the unaffiliated directors are furnished with sufficient information so as to enable them to participate effectively in the management of the investment company Fogel v Chestnutt supra at 745. In Gelfand v Chestnutt 402 F. Supp 1318 (1975) the District Court (S.D. New York) found that the investment adviser failed to furnish relevant financial information to the Fund's directors when consideration was being given to modifying the advisory contract to increase the expense ratio and that though the

desire to improve the profits of the investment adviser was, "perhaps not improper motivation" of the directors, but to do "without full disclosure and discussion" was inappropriate. The Court held

" While the financial stability of the adviser is a matter of legitimate concern to the Fund . . . Their only concern appears to have been that expenses were rising and they made the decision, in effect that the Fund, rather than the adviser should bear the burden of the increase."

In affirming the District Court the Second Circuit held that the investment adviser failed to furnish information "to enable the Fund's Board to evaluate the new contract" and that "the result of this dereliction was a patently one-sided revision of the advisory contract which placed the entire burden of rising costs and a falling market on the Fund, whose financial condition was not accorded even a passing concern" Gelfand v Chestnutt Corp. 545 F.2d 807,812 (1976).

An example of the type of information which was furnished to a board of trustees of a fund to enable them to evaluate an advisory agreement is demonstrated in the recent opinion of the Court in Gartenberg v. Merrill Lynch Asset Management, Inc. [Current] CCH Fed Sec. L Rep ¶98, 386 (S.D.N.Y. 1981) in which the court held that an investment adviser adequately informed the trustees so they could make an appropriate evaluation. The court found the trustees had received and carefully evaluated information concerning the structure of the fee, the going price in the market of comparable services, the nature of the

costs of the advisory services supplied, the scope of the services rendered, the performance achieved and the profitability of the contract overall. The court also found that the discussions appear to have been "frank and open".

In the instant case the record demonstrates that Mound and FMAC violated their fiduciary obligation to the funds and their shareholders by failing to furnish information of the type noted above and deemed by the courts to be sufficient to enable an evaluation of the terms of the contract whereby FMAC undertook to select, manage and supervise the portfolios of both funds. Mound and FMAC are found to have wilfully violated Section 15(c) of the 1940 Act.

Allegations Relating to Mound's Insider Trading Activity

Mound is charged with having caused FMAC to redeem shares of FMDI in December 1978 when he knew that the value of FMDI shares was overstated by approximately 5% and a substantial reduction of the reported net asset value of FMDI was imminent. The record discloses that on December 7 and 16, 1978 FMAC's vice-president prepared studies which reflected that FMDI's net asset value per share, based upon current market value of the portfolio instruments was \$.94 per share. These studies were circulated to all of the directors of the FMDI board. At a meeting of the board held on December 19, 1978 Mound advised the directors of FMAC's intention to liquidate the entire portfolio of FMDI and that such liquidation would reduce FMDI's net asset value from \$1.00 to \$.94.

On that same date Mound transferred \$28,000 from his wife's account at FMDI into his own FMDI account. Mound then transferred \$30,280 from his FMDI account into the FMDI account of FMAC, his advisory corporation. Mound then caused FMAC to redeem 30,280 shares of FMDI at a redemption price of \$1.00 per share. It is obvious that Mound and FMAC were aware since at least December 7, 1978 and knew for certain on December 19, 1978, when Mound advised the FMDI board that FMAC intended to liquidate the FMDI portfolio, that when the FMDI portfolio would be liquidated it would result in a reduction of the per share net asset value of the FMDI shares from \$1.00 to \$.94. Since Mound caused FMAC to redeem its FMDI shares on December 19, 1978, when he knew that the fund's current net asset value was overstated, the record supports the finding that he improperly avoided a loss of \$1,816.80. By such redemption FMAC and Mound received a disproportionate share of the fund's assets and shareholders suffered a disproportionate dilution of their investment. The record reveals that on December 20, 1978 FMAC liquidated the entire portfolio of FMDI and as a result FMDI incurred a capital loss of \$509,150 and the per share net asset value of FMDI was reduced to \$.94 per share.

The Commission and the Courts have held that corporate "insiders" particularly officers are prohibited from trading in their company's securities on the basis of material non-public



information acquired in the course of their corporate functions and that any such trading constitutes a violation of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. Cady Roberts & Co 40 SEC 907,912-916 (1961), SEC v Texas Gulf Sulphur Co 401 F.2d 833,847-48 (2d Cir. 1968)(en banc), cert denied sub-nom. Coates v SEC 394 U.S. 976 (1969). These cases teach that when a corporate insider has confidential information obtained as a result of his position he must refrain from trading until such information has become public. Even if the insider were in fact ignorant of the broad scope of the Rule and acted pursuant to a belief as to the applicable law such an ignorance does not imulate him from the consequences of his act. Tager v SEC 344 F.2d 5,8 (2 Cir. 1965). In the instant case Mound and FMAC, who were insiders as regards to FMDI's operation knew that the sale of its entire portfolio was imminent and would result in a reduction of the per share net asset value, nevertheless effected a redemption of their FMDI shares. It is concluded that by effecting such transactions Mound and FMAC wilfully violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

#### Additional Alleged Violations

Mound and FMAC are further charged with having wilfully violated and wilfully aiding and abetting violations of Section 30(d) of the 1940 Act. That section requires, among other things,

that a registered investment company transmit to its stockholders certain reports containing specified information, which reports shall not be misleading in any material respects. Earlier herein the conclusion was reached that Mound and FMAC approved and continued to permit the use of the amortized cost method of valuation of the portfolio securities of FMDI and that such conduct was in wilfull violation of the anti-fraud provisions of the Securities Act, the Exchange Act and the Advisers Act.<sup>32/</sup> The record reveals that FMDI sent its stockholders a "Third Quarter Report" for the nine months ended September 30, 1978 which reflected that FMDI valued the instruments in its portfolio at \$11,450,000. This figure was based on the continued use of the amortized cost method of valuation and overstated the fair value of such instruments by at least 2.6% and as much as 4.5%.

The record also reveals that by using the aforesaid method of valuation FMDI in its "Semi-Annual Report" to shareholders, for the six months ended June 30, 1978, valued its portfolio at \$11,940,384, a figure which overstated the current fair value of its assets by at least 1.4%. Similarly in its "First Quarter" report to shareholders for the three months ended March 31, 1978 FMDI valued its portfolio at \$12,800,000 which also overstated the current fair value of its portfolio. At the time these reports were sent to stockholders the respondents knew that the portfolio overstated the current market value of FMDI's portfolio. It is concluded that by continuing to employ

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<sup>32/</sup> See P. 23 supra

an improper method of valuation to value the instruments in FMDI's portfolio Mound and FMAC caused the current fair value of the said instruments to be overstated in the semi-annual and quarterly reports mailed to shareholders during 1978 in wilfull violation of Section 30(d) of the 1940 Act and aided and abetted violations by FMDI of the said Section.

The respondents are also charged with wilfully violating and wilfully aiding and abetting violations by FMDI of Rule 22c-1 of the 1940 Act. That section in substance, as pertinent here, prohibits a registered investment company issuing redeemable securities from selling or redeeming any such securities except at a price based on the current net asset value of such security. As a result of Mound's and FMAC's employment of an improper method of valuation to value the instruments in its portfolio, new investors in the shares of FMDI were caused to pay an inflated price for such shares while shareholders who redeemed shares of FMDI received a disproportionate share of the fund's assets. It is concluded that the respondents wilfully violated and wilfully aided and abetted violations by FMDI of Rule 22c-1 in that said respondents, by determining that FMDI utilize an improper method of valuation to value the FMDI portfolio instruments, caused shares of FMDI to be sold and redeemed at a price which exceeded the net asset value per share during 1978

#### Aiding and Abetting by Respondents

Respondents were found herein to have wilfully aided and

abetted violations of specified provisions of the securities acts. The Commission has held that "A finding that a person is an aider and abettor is established by a showing that he performed acts which he knows or has reason to know will contribute to the carrying out of the wrongful conduct." SEC v Gotham Securities 10 SEC Docket 895,898 (1976). The Courts have held that to hold a person as an aider and abettor it must be concluded "that a wrongful act occurred, that the defendant was aware of it, and that he knowingly and substantially participated in it." SEC v Falstaff Brewing Corporation et al 629 F.2d 62,72 (2d. cir), cert. denied, 449 U.S. 1012 (1980). The record establishes that in connection with the respondents' activities regarding the overstatement of the value of FMDI's portfolio, a wrongful act occurred, that the respondents were aware of it since at least from May 1977 when the Commission issued Release 9786 and that they knowingly and substantially participated in it. It is concluded that respondents wilfully aided and abetted violations by FMDI with respect to the use of the amortized cost method of valuation to value its portfolio.<sup>33/</sup>

#### Mound Acted With Scienter

Mound was found to have violated the anti-fraud provisions of the Securities Act (Section 17(a), the Exchange Act (Section 10(b) and Rule 10b-5 thereunder) and the Advisers Act (Section 206).

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<sup>33/</sup> Willfullness for these purposes does not require an intent to violate the law, but merely to commit the act which constitute the violation. See Tager v S.E.C. supra.

Although the Courts have held that proof of scienter is not required to establish violations of Sections 17(a)(2) and (3) of the Securities Act or Section 206(2) of the Advisers Act,<sup>34/</sup> the record demonstrates that Mound acted with scienter. The term scienter was defined by the Supreme Court to refer to a mental state embracing intent to deceive, manipulate or defraud. Ernst & Ernst v Hochfelder 425 U.S. 185,194n12 (1976). In attempting to ascertain whether Mound's mental state embraced an intent to deceive or defraud consideration is given to the fact that when the Commission issued its Release 9786 under the 1940 Act in May 1977 it stated it shall consider it inappropriate for money market funds to determine fair value of debt portfolio securities on an amortized cost basis, except in the case of securities with remaining securities of 60 days or less and that the use of that method of valuation cannot in the future represent a "good faith" effort to determine the "fair value" of portfolio securities for purposes of Rule 2a-4. The Commission further stated it expected companies to comply with the interpretation no later than November 1977.

As the record demonstrated Mound persisted in having FMDI continue in 1977 and 1978 to value its portfolio securities on the amortized cost basis when he knew that the fair market value of FMDI's portfolio had declined. He was concerned that shareholders would redeem their securities if the true value of the portfolio was revealed. Evidence of his fear of redemptions is his participation in the plan to have FMDI enter into undisclosed bank

<sup>34/</sup> Aaron v SEC 446 U.S. 680,697 (1980); SEC v Capital Gains Research Bureau, Inc., 375 U.S. 180(1963); Steadman v SEC 603 F.2d 1126(1979). Neither the language nor the legislative history of Section 30(d) or Rule 22c-1 of the 1940 Act suggests a scienter requirement.

loans in 1978 at interest rates which exceeded the rate of the return on its investments. Such conduct evinces a mental state embracing intent to deceive or defraud shareholders. At the very least, his failure to disclose the facts concerning FMDI's deteriorating financial condition during 1978 constitutes the type of reckless disregard for the interests of shareholders which satisfies any scienter requirement. Recklessness has been held sufficient to satisfy the scienter requirement. See e.g. Mansbach v Prescott, Ball & Turben, 598 F.2d 1017,1023-1025 (6th Cir 1979); Edward J. Mawod & Co. v SEC, 591 F.2d 588,595-597(10th Cir 1979); First Virginia Bankshares v Benson 599 F.2d 1307,1314(5th Cir 1977), cert denied 435 U.S. 952 (1978). It is concluded that Mound, in connection with his conduct regarding FMDI possessed the necessary scienter to establish his violation of the anti-fraud provisions of the securities acts noted above.

Similarly, in churning the portfolio of FMA for his personal profit, Mound acted with the necessary scienter or, at the very least, with the type of reckless disregard for the interests of shareholders which satisfies the scienter requirement.

#### Public Interest

The remaining question is whether it is in the public interest to impose sanctions upon Mound and FMAC. The findings that the respondents wilfully violated specified provisions of the securities acts have been detailed above and need no repetition here. An appraisal of the record suggests at least four aspects of Mound's conduct in connection with the operations of both funds which require scrutiny to determine whether sanctions are appropriate.

First, a perusal of Mound's conduct concerning the method of valuing the FMDI portfolio manifests a deliberate determination by Mound to continue the amortized cost method of valuation of the FMDI portfolio despite the Commission's release in May 1977 advising money market funds that such method was inappropriate and that it believes that the use of such valuation cannot in the future represent a "good faith" effort to determine fair value. In addition the Commission's statement that it expects companies to comply with the release no later than November 1977 was not accepted by Mound who, when he brought the Release to the attention of the board of directors of the fund, proposed a resolution that the fund continue its valuation policy. Such conduct evinces an attitude far from attempting to comply.

Second, Mound exhibited a lack of consideration of the effect of FMDI's valuation policy upon shareholders particularly in 1978 when that fund started experiencing mounting redemptions and a decline in the per share net asset value.

Third, an analysis of Mound's policies with respect to the manner in which he managed the portfolio of FMA leads to the conclusion that he was primarily motivated by his desire that FMA assure that FMAC, his advisory company, would be a profitable enterprise. This he accomplished by an excessive turnover of the portfolio which added substantially to the income FMAC was receiving and without concern for the effect of such practice upon shareholders. The record reveals that from 1975 through 1978 FMAC received four times as much revenue in the form of commissions as it received under its management agreement with FMA.

Fourth, Mound was primarily responsible for the concealment of the effect of the policies he pursued in the misrepresentations and lack of disclosure of such policies in the prospectuses and reports to shareholders, as detailed herein.

A final illustration that the primary interest which motivated Mound to use the funds for his personal profit is demonstrated by his action in causing FMAC to redeem its shares in FMDI on the very day he advised the FMDI board of directors of FMAC's intention to liquidate the entire portfolio of FMDI and that such liquidation would reduce the per share net asset value of the fund from \$1.00 to \$.94. With knowledge that the fair value of the FMDI shares was less than \$1.00 he nevertheless caused his advisory corporation to redeem its shares at \$1.00 without regard for the fact that he was receiving more than fair value for his shares, that purchasers of his shares would be paying more than the fair value and that remaining shareholders would suffer a dilution. Such insider trading tactics should not be encouraged by permitting persons who engage therein to act in an advisory capacity to a fund.

All of these factors demonstrate Mound acted with a blatant disregard of the fiduciary obligations he had to the shareholders of each of the funds. Mound's conduct eventuated in the type of violations which were found to constitute a



course of business which operated as a fraud and deceit upon shareholders and prospective purchasers and the employment of devices and artifices to defraud.

In light of the evidence supporting the serious and pervasive violations found herein and the record adduced in these proceedings, it is concluded that the sanctions ordered below are appropriate and essential in the public interest.

ORDER

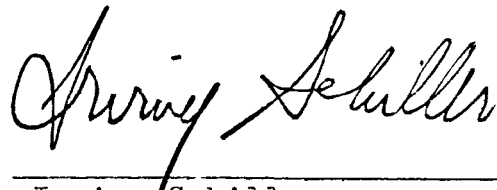
IT IS ORDERED that Milton Mound and First Multifund Advisory Corp. are hereby barred from serving or acting in any of the capacities specified in Section 9(b) of the Investment Company Act of 1940.

IT IS FURTHER ORDERED that the registration of First Multifund Advisory Corp. as a broker-dealer is hereby revoked.

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

Pursuant to Rule 17(f), this initial decision shall become the final decision of the Commission as to each party that has not within fifteen(15) days after service of this initial decision upon him or it, 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 or it. 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.<sup>35/</sup>



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Irving Schiller  
Administrative Law Judge

Washington, D.C.  
December 29, 1982

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<sup>35/</sup> All proposed findings, conclusions and supporting arguments of the Division have been considered. To the extent that the proposed findings and conclusions 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 the various witnesses is not in accord with the findings herein, it is not credited.