ADMINISTRATIVE PROCEEDING
FILE NO. 3-4403

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of

PETER CAPLIN
GOTHAM SECURITIES CORPORATION
N. CARROLL MALLOW

INITIAL DECISION

July 21, 1975
Washington, D.C.

Irving Schiller
Administrative Law Judge

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APPEARANCES: Allan M. Lerner, Harry L. Garmansky and Janice Handler Attorneys, New York Regional Office and Harold Halpern Washington, D.C. for the Division of Enforcement.

Barry Feiner and Paul Chernis of Feiner, Curtis, Smith and Goldman, New York, New York, for Respondents Peter Caplin and Gotham Securities Corporation.

Sol Friedman, New York, New York for respondent N. Carroll Mallow.

BEFORE: Irving Schiller, Administrative Law Judge

This proceeding was instituted by an order of the Commission dated December 11, 1973 ("Order") pursuant to Section 15(b), 15A and 19(a)(3) [1/] of the Securities Exchange Act of 1934 ("Exchange Act") to determine whether various named respondents [2/] wilfully violated certain specified provisions of the Securities Act of 1933 ("Securities Act") and the Exchange Act and Rules thereunder, to determine further whether certain of the respondents failed reasonably to supervise persons subject to their supervision with a view to preventing their commission of the violations alleged in the Order and, finally, to determine whether any remedial action might be appropriate in the public interest.

1/ 15 U.S.C. §78o(b); 15 U.S.C. § 78o-3; 15 U.S.C. §78s-3.

2/ The Commission has accepted offers of settlement from the following named respondents and has issued its findings and orders imposing remedial sanctions: Park Securities, Inc. and Daniel J. Claridy, Exchange Act Release No. 11077, October 30, 1974, 5 SEC Docket 355; Richard Pinto, Exchange Act Release No. 11235, February 11, 1975, 6 SEC Docket 263; Martin Demsky, Exchange Act Release No. 10865, June 10, 1974, 4 SEC Docket 472; Robert Pile, Exchange Act Release No. 10758, April 26, 1974, 4 SEC Docket 198; Harris Upham & Co. Incorporated, Exchange Act Release No. 10930, July 26, 1974, 4 SEC Docket 629; Ciro Cozzlino and Steve Harris, Exchange Act Release No. 11012, September 13, 1974 5 SEC Docket 152. Although this initial decision has no application to the aforementioned respondents one or more of them may be mentioned herein in light of the nature of the allegations in the Order relating to the respondents who are the subject of this decision.

In connection with the allegations against respondent N. Carroll Mallow reference is made to the Commission Order Inviting Briefs dated June 27, 1975 in which the Commission notes, among other things, that the Securities Act Amendments of 1975 raises questions as to the present status of cases instituted under the Exchange Act as it stood before June 4, against people who are not alleged to have been broker-dealers or persons seeking to become so associated. The Order invites respondent Mallow and others to file a brief with the Commission on the impact, if any, of the new statute on cases brought under former Section 15(b)(7). Accordingly, this decision will not consider the allegations against Mallow pending further order of the Commission. See Exchange Act Release No. 11500, June 27, 1975.

The Order, among other things, alleges that respondents Peter Caplin ("Caplin") and Gotham Securities Corporation ("Gotham"), singly and in concert with other named respondents wilfully violated and wilfully aided and abetted violations of the anti-fraud provisions contained in Section 17(a) of the Securities Act and Section 10(b)(5) of the Exchange Act and Rule 10b-5 thereunder in connection with the offer, sale and purchase of units (hereinafter referred to as "units" or "securities") of Bolton Group, Ltd. ("Bolton").

Specifically Caplin and Gotham are charged with entering into arrangements with Park Securities Inc. ("Park") and other named respondents whereby Gotham inserted quotations in the "pink sheets" 3/ at prices determined by Park, and traded Bolton securities pursuant to a guaranteed profit thereby creating a false and misleading appearance concerning the widespread nature, depth, freedom and independence of the market for such securities. Caplin and Gotham are also charged with making false and misleading statements of material fact and omitting to state material facts concerning the investment merit, present and prospective demand for, price, value and market for Bolton securities as well as the financial condition, business operations and prospects of the said company. Additionally, the said respondents are charged singly and in concert with Park and other named respondents with wilfull violations of the anti-manipulative provisions of Section 15(c)(2) of the Exchange Act and Rule 15c2-7 thereunder 4/ in that

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3/ Published by the National Quotation Bureau, Inc.

4/ 15 U.S.C. §78o(c)(2); 17 CFR §240.15c2-7.

quotations for the securities of Bolton and EKG Service Corp. ("EKG") were furnished to an inter-dealer-quotation system in furtherance of a guaranteed profit, without the inter-dealer-quotation system being informed of the said arrangement and without other brokers or dealers submitting quotations for the said securities in the aforementioned system being informed of said arrangements.

After appropriate notice, hearings were held before the undersigned. Proposed findings of fact, conclusions of law and supporting briefs were filed by counsel for the Division of Enforcement and respondents Caplin and Gotham.

The following findings and conclusions are based upon a preponderance of the evidence as determined by the record and upon observation of the demeanor of the various witnesses.

The Respondents

Gotham has been registered as a broker-dealer with the Commission pursuant to Section 15(b) of the Exchange Act since December 7, 1969. The Order alleges Gotham is a member of the National Association of Securities Dealers Inc. (NASD)[5/], a national securities association registered pursuant to Section 15A of the Exchange Act. Gotham's principal place of business was in New York, New York.

In 1969 Caplin was an officer, director and shareholder of Gotham. In March 1971 Caplin became president of Gotham and owned in excess of 75% of Gotham's common stock.

5/ Official notice is taken of NASD press Release of December 30, 1974 NSD21274 p. 10, which states that Gotham was expelled from membership in the Association for failure to pay the fine and costs assessed in connection with findings of violations of the Rules of Fair Practice of the Association.

Bolton and EKG

The charges in this proceeding relate to Gotham and Caplin's activities in connection with sale of securities of Bolton and the common stock of EKG. The Order alleges that on June 14, 1972 Bolton filed a notification and offering circular for a public offering of 100,000 units of Bolton at $1.25 per unit, pursuant to Regulation A under the Securities Act. Park was named as underwriter. The Form 2-A report filed by Bolton on May 4, 1973, represented that Park had sold the 100,000 units in the period September 1, 1972 to October 6, 1972. By order dated June 18, 1974, the Commission permanently suspended the Regulation A exemption of Bolton.[6/] The Order also alleges that on June 28, 1972 EKG filed an notification and offering circular for a public offering of 100,000 shares of its common stock at $5.00 per share, pursuant to Regulation A under the Securities Act. Park was also named as underwriter. The Form 2-A report filed by EKG on April 30, 1973 represented that Park had sold 33,333 shares between October 10, 1972 and December 29, 1972. The Form 2-A states that Park informed EKG it was unable to sell more than the minimum offering. By order dated June 18, 1974, the Commission permanently suspended the Regulation A exemption of EKG.[7/]

6/ 4 SEC Docket 499.

7/ id.

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

The gist of the charges against Caplin and Gotham with respect to the Bolton securities are that they entered into arrangements with Park whereby Gotham inserted quotations in the pink sheets, an inter-dealer quotation medium, at prices determined by Park and purchased and sold the Bolton securities, pursuant to a guaranteed profit thereby creating a false and misleading appearance concerning the nature, freedom and independence of the market for such securities. A narration of the circumstances which eventuated in Gotham's inserting quotations in the pink sheets for the Bolton securities and a perusal of the Bolton transactions between Park and Gotham will be of material assistance to an understanding of the nature of the alleged violations.

In August 1972 Caplin employed one George C. Bergleitner, Jr. ("Bergleitner") as a trader and a registered representative for Gotham.[8/] In the early part of October 1972, Bergleitner received a telephone call from Richard Pinto ("Pinto"), an old college acquaintance, who informed him that a Mr. Dan Claridy ("Claridy")[9/] head of Park, had a new issue he was coming out with and wanted somebody to trade the stock. Shortly thereafter Bergleitner received a call from Claridy who, after identifying himself as head of Park, stated he was coming out with an underwriting of something called Bolton and inquired whether Bergleitner would like

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8/ Prior to his employment by Gotham, Bergleitner was employed in the brokerage business for approximately fifteen years. He was a principal in two brokerage firms, G.A. Equities Corp. and M.J. Manchester & Co.

9/ The reference was to Daniel J. Claridy (See footnote 2).

to trade the stock. Claridy told Bergleitner the stock would be coming out shortly and that "we could make a lot of money in the stock." Bergleitner testified that Claridy also said he would "protect us in the stock and he would cover all my shorts and fill me with all my longs." Bergleitner further testified that when Claridy assured him that he would be "protected" it was his understanding that when Park would pick up the shorts or supply the longs, Gotham would make a profit of an eighth of a point if the stock was selling below $5 and a fourth of a point if the stock was over $5. In light of the documentary evidence of the transactions between Park and Gotham, as noted below, Bergleitner's understanding was correct.

Either the day of the above talk or the next day Bergleitner told Caplin he had been referred to Claridy by Pinto, that Park was coming out with a new issue, that Claridy wanted Gotham to trade the stock and that Claridy would take Gotham's longs and cover its shorts. Caplin asked Bergleitner "if we could get hurt in the stock" and Bergleitner told him "we wouldn't get hurt and that we had protection."

Bergleitner talked with Claridy on at least one other occasion prior to his first trade. In his second call Claridy alerted Bergleitner the issue was breaking and it was time to go into the sheets.

Bergleitner testified he obtained Caplin's approvel to insert quotations in the pink sheets and that Caplin left the details entirely in his hands. Caplin also gave Bergleitner approval to trade the Bolton securities again leaving the details of the day to day trading in Bergleitner's hands.

Bergleitner further testified that pursuant to his arrangement with Claridy he would call Claridy in the morning before he started trading to ascertain the prices at which Gotham would trade the Bolton securities. Additionally, Bergleitner would call Claridy during the day, depending on volume of trading, for instructions as to the quantity of purchases or sales which Gotham should consummate. When asked whether he discussed the price of Bolton stock with Claridy, Bergleitner testified "I called him frequently to see what the quotation was, what he would like, what quote they were giving out away from me." And when questioned as to whether he used the prices obtained from Claridy as a guide Bergleitner replied "yes, I keyed on him."

Thereafter, and pursuant to the above arrangement, Gotham entered bid and ask quotations for the Bolton securities in the pink sheets and effected purchases and sales of the said securities. Generally, as described by Bergleitner, when a call was received from a broker desiring to effect a trade, he would put the caller on hold, phone Claridy for instructions as to whether Gotham should consummate the transaction, and act accordingly. Thus, for example, the record discloses that on October 10, 1972 when Bergleitner received a bid for 500 shares of Bolton from a firm in Providence, Rhode Island, he immediately called Claridy, told him of the bid and asked if he wanted to sell five hundred. Claridy told Bergleitner to sell only two hundred

units. Bergleitner followed Claridy's instructions and sold only 200 units.[10/]

The record discloses that in each instance during the period October 10, 1972 to January 10, 1973, when Gotham sold Bolton units to another broker-dealer[11/] he purchased an equivalent amount of the said securities from Park either the same or next business day, at a profit of either an eighth or a quarter of a point. When Gotham purchased Bolton from other broker-dealers he sold such securities in each instance to Park the same or next business day at a similar profit.

The record further discloses that on January 12, 1973 Gotham purchased 100 Bolton units from a broker-dealer firm and sold them to Park. Confirmation of the sale was received by Gotham. However, on January 15th 1973 Park failed to honor the trade and refused delivery of the stock. Several attempts were made to deliver the stock but Park refused to accept delivery.

The above findings relating to the arrangement between Claridy and Bergleitner and Caplin's knowledge and approval thereof, pursuant to which Gotham purchased and sold the Bolton securities at a guaranteed profit to Gotham, is premised upon the testimony of Bergleitner and the documents supporting such testimony in the record. When called as a

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10/ As an example of the manner in which the Gotham and Park transactions were consummated under the arrangement, the documentary evidence shows the following: On October 10, 1972 (as noted in the text) Gotham sold 200 Bolton units at 2¼ to the brokerage firm in Providence, Rhode Island. On October 11, 1972 Gotham purchased 200 Bolton units from Park at 2 1/8. That same day Gotham sold 300 Bolton units at 3 to a brokerage firm and purchased a similar amount from Park at 2 7/8. Thus, under the arrangement, Gotham realized a profit of 1/8 of a point on each of its transactions.

11/ All of the transactions were with other broker-dealers. There is no evidence that Gotham sold Bolton to retail customers.

witness by the Division Caplin declined to testify, basing such refusal upon his right to due process of law as guaranteed by the Fifth Amendment to the Constitution of the United States and the appropriate provisions provided by the Administrative Procedures Act. The record clearly shows that Caplin's refusal to testify was not based upon his fear of self-incrimination, which he specifically excluded from his statement, but solely upon the due process clause of the said Amendment. His sworn testimony given to Commission investigators during the investigation prior to the commencement of these proceedings was thereupon received in evidence.[12/]

Caplin's prior investigative testimony merely corroborates Bergleitner's testimony as to Caplin's knowledge and approval of the arrangement between Claridy and Bergleitner. Thus, the record reveals that Bergleitner's testimony that he obtained Caplin's approval to insert quotations and trade the Bolton securities is substantiated by Caplin's testimony that Bergleitner "represented to me" that Park wanted "Gotham to put a quotation into the pink sheets and trade the stock at pretty much at their direction" and that ". . . if we became short they would fill our short. If we acquired a long position they would buy our long position." Caplin's prior investigative testimony further reveals his knowledge of the profit arrangement between Claridy and Bergleitner. Caplin testified "I specifically asked Mr. Bergleitner at the time: 'Are we protected in this, because I don't feel like picking up somebody else's trading numbers who we don't know anything about.'"

12/ With respect to Caplin's argument that his investigative transcript was improperly obtained see discussion commencing at page 19 infra.

Bergleitner's testimony above as to the conversations he had with Claridy relating to the arrangement concerning the Bolton units together with his testimony that he relayed such conversation to Caplin and obtained Caplin's approval to go into the pink sheets and to initiate trading in the Bolton units remains unrefuted and is credited. Moreover, it is clear from the record that Caplin was, during the relevant period, responsible for Gotham's operations and reviewed Gotham's positions with Bergleitner each evening to be certain the firm's position in Bolton would pose no threat to Gotham's capital. Wholly apart from his investigative testimony it appears evident from the record that Caplin should have been alerted as to the existence of the arrangement. Thus, by looking at the confirmation of the transactions each evening Caplin should have become aware or, at the very least, should have realized, that Park was always on the other side of all transactions in Bolton, and always at an eighth or quarter point profit. Any reasonable inquiry by Caplin would have revealed the arrangement between Park and Gotham pursuant to which Bergleitner was consummating the transactions. All of the foregoing circumstances should have placed Caplin on notice that he might be lending himself and Gotham to participating in a fraudulent scheme or device and that, at the least, they were thereby under an obligation to exercise the greatest care. This they failed to do.

In light of all of the circumstances, including the trading pattern between Gotham and Park with respect to the Bolton securities, it is concluded that Park, Caplin and Gotham entered into an arrangement for the

insertion of quotations in the pink sheets at prices determined by Park and purchased and sold the Bolton securities pursuant to a guaranteed profit.

Respondents urge there is nothing in the record to support the proposition that if Gotham had not entered quotations in the pink sheets, the market in the Bolton securities would have acted or appeared any differently than it did . The argument is purely speculative and without merit. The record disclosed that, in fact, Gotham entered quotations in the pink sheets at the request of Park and at prices determined only after Bergleitner talked with Claridy and was advised what prices the latter wished to insert at the particular time. Commencing with the initial sale, as noted above, on October 10, 1972 at 2¼ for 200 shares, the record shows that the following day Gotham sold an additional 300 shares at 3. During the month of November 1972 Gotham consummated purchases and sales of approximately 3,100 Bolton units at prices ranging from 4 3/8 on November 14, to 8 on November 30, 1972. There is no evidence in the record as to Bolton's business operations or financial condition which could have accounted for the sharp increase in the price of its securities. Nor is there any evidence, as suggested by respondents, that supply and demand determined the market price. Caplin and Gotham knew or should have known that the manner in which the Bolton transactions were effected was not the result of a free and independent market and that there was no basis for their trading at substantially increased prices

particularly where such prices could not be related to the investment value of such securities. In this connection it is noted that in its release announcing the proposal to adopt Rule 15c2-11, the Commission pointed out that "the hasty submission of quotations in the daily sheets . . . . in the absence of information about the security or the issuer" in many cases resulted in an irresponsible "numbers" game which is "not only disruptive of the market but fraught with manipulative potential."[13/]

The "potential" with which the Commission was concerned in its release became a manipulative reality in the instant case. Respondents offered no proof that they inserted quotations in the pink sheets because of any knowledge of the issuer or the belief that the market price of the Bolton securities which Gotham was inserting in the sheets represented the value of such securities. To the contrary, the record clearly shows Gotham was, during the relevant period, receiving instructions as to the prices to quote as well as the prices at which it should consummate transactions and the amounts of securities it should purchase or sell. It is concluded that Gotham wilfully violated and Caplin aided and abetted violations of the anti-fraud provisions of the Securities Acts by inserting quotations in the pink sheets at prices determined by Park and Claridy and effecting transactions pursuant to a guaranteed profit, thereby creating the false and misleading appearance concerning the nature, depth, freedom and independence of the market for the Bolton securities.

Caplin and Gotham are also charged with making untrue statements of material facts and omitting to state material facts in connection with the purchase and sale of the Bolton securities, concerning the investment merit

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13/ Securities Exchange Act Release No. 8909 (June 24, 1970).

of Bolton, the present and prospective demand for, price, value and market for such securities, and the financial condition, operation and prospects of Bolton. No evidence was presented that Caplin made any such affirmative statements of material fact in connection with purchases and sales of the Bolton securities, nor was evidence presented that Bergleitner made any such statements on Gotham's behalf. It is concluded that such allegations have not been proven. Accordingly, such charges are dismissed. However, the evidence shows that Bergleitner, as trader for Gotham sold the Bolton securities, without disclosing to the broker-dealer customers the arrangements Gotham had made with Park for the insertion of quotations in the pink sheets at prices dictated by Park nor was disclosure made of the guaranteed profit as described above. As a broker-dealer Gotham had a duty to make an adequate disclosure to its customers concerning its arrangements with Park. In Affiliated Ute Citizens v. United States, 406 U.S. 128, 153 (1972) the Supreme Court in considering the criteria of Section 10(b) of the Exchange Act and Rule 10b-5 noted that the said Rule, among other things, makes it unlawful for any person, directly and indirectly to omit to state material facts or to engage in acts or practices which operate or would operate as a fraud or deceit upon any person and held:

> "All that is necessary is that the facts withheld be material in the sense that a reasonable investor might have considered them important in the making of this decision. See Mills v. Electric Auto-Lite Co., 396 U.S. 375, 384 (1970); SEC v. Texas Gulf Sulphur Co., 401 F. 2d 833, 849 (C.A. 2, 1968), cert. denied sub nom. Coates v. SEC, 394 U.S. 976 (1969); 6 L. Loss, Securities Regulation 3876-3880 (1969 Supp. to 2d ed. of Vol. 3); A. Bromberg, Securities Law, Fraud — SEC Rule 10b-5, §§2.6 and 8.6 (1967). This obligation to disclose and this withholding of a material fact establish the requisite element of causation in fact. Chasins v. Smith, Barney & Co., 438 F. 2d, at 1172."

In the instant case it is concluded that Bergleitner's failure to disclose the arrangements with Park constituted material omissions within the meaning of Rule 10b-5, and such omissionswere in wilfull violation of the anti-fraud provision of the Securities Acts. Since Bergleitner was an employee of Gotham, the latter must be held to have committed the anti-fraud violations engaged in by Bergleitner on the principle of respondeat superior. S.E.C. v. Management Dynamics Inc., ____ F. 2d____, (C.A. 2, 1975), CCH Fed. Sec. L. Rep. ¶95,017, pp. 97,562, 97,571; Sutro Bros. Inc., 41 S.E.C. 470, 479 (1963). Gotham by engaging in the activities described above, is also found to have engaged in acts and practices which operated as a fraud, as charged in the Order.

The record contains no evidence that Caplin personally consummated any of the purchase or sale transactions. It is concluded that the charges alleging that Caplin wilfully violated the antifraud provisions of the securities laws by omitting to state material facts in connection with the Bolton transaction, have not been proven. Accordingly, such charges are dismissed.

Violation of Section 15(c)(2) and Rule 15c2-7

As noted earlier Caplin and Gotham are charged, singly and in concert with others, including Claridy and Park, with having violated and aided and abetted violations of Section 15(c)(2) of the Exchange Act and Rule 15c2-7 thereunder. In essence they are charged with furnishing quotations for securities of both Bolton and EKG to an inter-dealer quotation system without informing such system of the guarantee of profit arrangement described above with respect to Bolton, or of a similar arrangement which was made with EKG as described below, and without informing other broker-dealers submitting quotations for the said securities in the system of the arrangements. Section 15(c)(2) of the Exchange Act, in pertinent part, prohibits a broker or dealer

from effecting any transation or inducing or attempting to induce the purchase or sale of any security in the over-the-counter market, in connection with which such broker or dealer makes any fictitious quotation. The Section requires the Commission, by rules and regulations to define, among other things, such quotations as are fictitious. The Commission promulgated Rule 15c2-7 14/ and defined what shall constitute an attempt to induce the purchase or sale of a security by making a "fictitious quotation" within the meaning of the above Section. As applicable to the instant case, the Rule provides that where a broker or dealer furnishes or submits, directly or indirectly, any quotation for a security to an inter-dealer-quotation system in furtherance of one or more arrangements, including, among other things, a guarantee of profit or guarantee against loss, it will be considered a "fictitious quotation" unless the inter-dealer system is informed that the quotation is furnished or submitted in furtherance of the arrangement between or among brokers and dealers together with the identity of each broker or dealer participating in such arrangement, unless only one of the participating broker-dealers submits a quotation. In its release accompanying the adoption of the aforesaid Fule, the Commission acknowledged that the "pink sheets" referred to herein published by the National Quotation Bureau Inc. is considered an inter-dealer-quotation system.

In the preceding section dealing with the antifraud violations, the manner in which Gotham commenced inserting quotations in the pink sheets with respect to the Bolton securities was detailed. The understanding reached between Claridy for Park, and Bergleitner for Gotham, that Park would cover Gotham's shorts and purchase its longs, that Gotham would be guaranteed a profit on each trade and that Gotham would not be hurt was well

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14/ Securities Exchange Act Release No. 7381 (August 6, 1964).

within the meaning of the word "arrangement" as contemplated be the aforesaid Rule. The existence of the arrangement is amply corroborated by the documentary evidence which reflects that Park consistently supplied Bolton securities to Gotham to cover its shorts and bought Gotham longs and that on each of such transactions Gotham realized a profit of, at least, 1/8 of a point. The record contains no evidence that any disclosure was made to the inter-dealer-quotation system of the arrangement. A perusal of the quotations in the pink sheets for the Bolton securities for the period October 9th through at least November 30th, 1972 reveals that both Park and Gotham inserted quotations on particular days and that no appropriate symbol appeared in the sheets reflecting any arrangement.

With respect to the EKG stock, Bergleitner testified that in the latter part of December 1972 he was called by Claridy who told him that Park was "doing another underwriting . . . . for EKG and he would like me to trade it." Claridy also told him that there would be protection, that Gotham would not get hurt, that the stock would do much better in the after market and that it should go to $7 or $8. In addition,Claridy offered Park a selling group participation in EKG. Bergleitner told Caplin of his conversation with Claridy and that "it was the same deal as Bolton Group." When Caplin asked if Park could be trusted Bergleitner told him that Claridy "did a good job on Bolton Group, they are probably going to do the same thing on EKG." Bergleitner requested and received Caplin's permission to insert quotations in the pink sheets. Caplin asked if "we could get hurt on the stock"

and Bergleitner informed him, "no, we have the same protection as we did on the Bolton Group. We didn't get hurt in that." Thereafter, Gotham received word from Park to enter quotations in the pink sheets and as, in the Bolton situation, followed those instructions. An examination of the pink sheets for the month of January 1973 reveals that on particular days both Park and Gotham inserted quotations therein and that no appropriate symbol appeared reflecting any arrangement.

In an explanatory release accompanying the adoption of the text of the above mentioned Rule[15/], the Commission, as pertinent here, clearly and unequivocally stated "The rule also requires that, where two or more broker-dealers place quotations in the sheets pursuant to any other arrangement between or among broker-dealers, then the identity of each broker-dealer participating in any such arrangement or arrangements, and the fact that an arrangement exists must be disclosed. . . ; the purpose of the rule is to cover any arrangement between broker-dealers, such as : . . guarantees of profit, guarantees against loss. . . ." The record amply supports the finding that there was an arrangement between Park and Gotham whereby Park covenanted to cover Gotham's shorts in Bolton and EKG and purchase its longs in both securities and guaranteed Gotham a profit and/or guaranteed it against loss. Having failed to disclose the agreement to the inter-dealer-quotation system, Gotham wilfully violated and wilfully aided and abetted violations of Section 15(c)(2) and Rule 15c2-7. The record evidences that Caplin gave Bergleitner authority to insert quotations in the pink sheets for Gotham with respect

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15/ See footnote 14 *supra*.

to both the Bolton and EKG securities and that at the end of each day reviewed Bergleitner's transactions. Caplin knew or could have easily ascertained the existence of the arrangements and the guarantees of profits. Caplin is thus found to have wilfully aided and abetted Gotham's violations of the above mentioned Section and Rule.

Respondents urge that the above mentioned Commission release speaks of a quotation submitted "on behalf of" another broker-dealer "thus presupposing that Caplin was not master of his own house as to price, timing and insertion." Respondents also urge that the so-called "arrangement" and guarantee were neither effective nor effectuated. The arguments lack validity and are not supported by the record. The above quotation from the release appears in connection with a discussion of a situation where a broker-dealer is a correspondent for another firm for a particular security and enters quotations in the sheeets. Since the instant case does not involve a quotation by a correspondent firm, the above quoted portion of the release is irrelevant.

With respect to the argument as to Caplin's purported independence, the record discloses that Botham's trader called Park in the morning before trading started to ascertain what the market price should be, what Park would like and used the information as a guide to determine what to do. The record further reveals that Gotham's trader checked with Park prior to effecting any transaction in Bolton or EKG securities. Thus a finding that Caplin, in fact, "was not master of his own house as to price, timing and insertion" is supported by the record. In light of the profits realized by Gotham, the record fails to support respondents' contention that the guarantees were neither effective nor effectuated.

Respondents' Claims of Lack of Fairness and Due Process

Caplin and Gotham urge that the evidence against them is premised on the testimony given by Caplin and Bergleitner during the investigation conducted by the staff concerning the Bolton and EKG securities. Respondents assert that such testimony was obtained upon the promises made by the staff of the Commission that neither Caplin nor Gotham would be named as a respondent in any enforcement proceeding, that Caplin was given immunity and waived his Fifth Amendment privilege against self incrimination. Caplin also maintains he induced Bergleitner to testify on the assurance that the staff had no interest in Caplin or Gotham.

Prior to commencement of the hearings, the respondents moved to dismiss these proceedings upon the same grounds presently being urged. The Division filed affidavits admitting that prior to the taking of Caplin's testimony, respondents were advised by the regional office of the Commission that it would not recommend that Caplin or Gotham be named as respondents. However, the Commission, in its order denying the motion stated, among other things, that in fact, the regional office did not recommend that respondents be named but that recommendation was made by the headquarters staff in Washington. However, the order states, respondents' counsel, a former staff enforcement attorney, not only knew that final decision on whether respondents would be named did not rest with the regional office, but was explicitly warned that the

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16/ Order Denying Motion to Dismiss, dated May 9, 1974.

aforementioned recommendation was subject to review by the Staff's superiors in Washington.

During the course of the hearings evidence was taken with respect to the respondents' claim of unfairness and lack of due process in obtaining both Caplin's and Bergleitner's testimony. Such evidence fully supports the Commission's conclusions that respondents' contentions lack substance. To fully appreciate the conclusions reached herein on the basis of the entire record a review of the evidence appears essential.

Prior to the institution of these proceedings an investigation was conducted by the staff as an outgrowth of a joint SEC-NASD Joint Task Force. One, Michael Harris ("Harris") was New York coordinator of the Task Force. Assigned to the investigation were Margaret McQueeney ("McQueeney"), an investigator, Harold Halpern ("Halpern"), a staff attorney, and Harold Brown, an NASD staff investigator. Harris reported to Irwin Borowski who was then Chief Enforcement Attorney, presently an Associate Director of the Division. These facts are not disputed.

In April 1973, the staff conducting the investigation determined that Caplin should be questioned concerning Gotham's involvement in the Bolton transactions and at the staff's request, Marc N. Epstein, ("Epstein") who was Caplin's attorney at the time, met with staff to explore the matter. What transpired at this meeting between Harris and Epstein, at which McQueeney was present, is of crucial significance since Caplin's claims are premised upon his understanding of what was said at that time. Harris informed Epstein that in reviewing Gotham's trading in the Bolton securities there appeared to be a manipulative pattern and indicated that Caplin's

testimony and his knowledge of the transactions could be of help. In response to Epstein's inquiry concerning Caplin's status if he agreed to testify, Harris informed him that in view of the fact that another investigation in which Caplin and Gotham were involved, and one in which Epstein was also representing Caplin, would in all likelihood result in sanctions against Gotham and Caplin, Harris felt there appeared to be no compelling reason to include Caplin and Gotham as respondents in the instant proceeding since the public interest would be served by any sanctions in the other proceedings. Epstein was of the same view.

McQueeney testified that Harris made it quite clear at that meeting that the recommendations of the Task Force were subject to review by higher authority in the New York Regional Office and told Epstein specifically that ultimate review by Borowski would occur before any recommendation would be forwarded to the Commission. McQueeney further testified she believed that Epstein fully understood that no promises of immunity were tendered to either Caplin or Gotham. Her understanding of Epstein's knowledge was based upon three factors; (1) that no statement was made by Harris or hereself to the effect that Gotham or Caplin would be offered "immunity," since neither had such authority; (2) that she knew that Epstein was a former staff attorney who was well aware that people on the staff level "don't go around making promises to proposed witnesses before they even have given testimony" and (3) that proceedings against Park were not imminent. Vigorous cross-examination failed to alter or vary the witnesses recollection of the meeting. Respondents did not call Epstein to refute McQueeney's testimony.

The record supports McQueeney's testimony. When Caplin appeared on May 1, 1973, to testify in the investigation, he was represented by Epstein and after being sworn, was advised, on the record, of his constitutional privilege to refuse to answer any questions and reminded of such privilege when he again testified on May 25, 1973. There is no statement in the transcript by Caplin that he was testifying becuase of any grant of immunity[17/] nor did Epstein make any such statement for the record. Thereafter, the staff forwarded the investigative file to the headquarters office in Washington and did not recommend that Gotham or Caplin be named as respondents. However, when the file was reviewed by Borowski, the latter disagreed and determined that Caplin and Gotham should be named as respondents. Borowski conferred with Halpern who stated he had not intended to recommend the inclusion of Gotham and Caplin as respondents. When told by Borowski that the recommendation was unacceptable, Halpern stated that he had promised Epstein to advise him if Washington disagreed with Halpern's recommendation. Borowski authorized Halpern to inform Epstein of the decision and Halpern did so. Shortly thereafter, Epstein called Borowski stating he wished to make a submission to the Commission on behalf of his clients before the Commission acted on Borowski's recommendation. Borowski agreed to present the submission to the Commission.

17/ It is of interest to note that the staff is well aware of the manner in which immunity may be granted. During the course of the investigation the staff, when informed by another prospective witness, whose testimony was considered necessary and appropriate, that he would refuse to testify on the basis of the privilege afforded by the Fifth Amendment, obtained a Commission order pursuant to Title 18, Sections 6002 and 6004 of the United States Code, compelling said witness to testify. It is logical to conclude that in the case of Caplin the staff did not intend to confer immunity.

By letter dated December 4, 1973 Epstein informed the Commission, among other things, of his meeting with Harris and McQueeney in which they sought his clients' help in the investigation. Epstein stated he was informed "that if such cooperation were forthcoming, it would be given large consideration in framing an appropriate recommendation." Of utmost significance is a portion of the letter which not only reveals the direct clue to the understandings between Epstein and the staff but substantiates McQueeney's testimony as to her recollection of the meeting referred to above and exposes the lack of substance of respondents' contentions. On page 4 of his letter Epstein advised the Commission that the staff stated it was "not interested" in bringing any action against Caplin or Gotham. As a footnote to the said sentence Epstein in unequivocal language states:

> "It is not contended that the Staff made any promises of a binding nature in this matter. But it is contended that the cooperation of Caplin was of utmost importance to the Staff and therefore, to them, outweighed the need for recommending any enforcement action against Caplin and Gotham. It is in this sense that I interpret the phrase 'not interested'".

Caplin testifying as to his so-called understanding of the meeting, stated that Epstein told him that Harris said that the staff was interested in seeking Caplin's cooperation in an investigation involving Bolton. Caplin also testified he told Epstein he was concerned as to what his and Gotham's involvement would be and wanted to know whether it would be possible to receive immunity before giving any testimony. In that connection it is noted that Caplin in his motion to dismiss these proceedings, as noted above, filed an affidavit in support of the motion

in which he states "Based on statements of the SEC as relayed by my counsel, I believed that if I cooperated with the SEC as they urged me to I would have full immunity." Caplin merely expresses his own belief but does not say specifically that Epstein said that Harris, or any other staff member, had promised him immunity. When asked as to the reasons for the omission Caplin testified that he discussed the matter with his present counsel and "we decided that even though I had inadvertently left it out of my prior affidavits, since it was the truth I should bring it up." His testimony as to his reasons is not credited since it varies with his earlier affidavit and more importantly, the promise of immunity by the staff is not mentioned by his former counsel when he submitted his letter to the Commission in December 1974, in the attempt to have Caplin and Gotham omitted as respondents in these proceedings. Caplin further testified that when he read Epstein's letter to the Commission he believed that the statement on page 4, quoted in the text, was incorrect, but he made no attempt to so advise the Commission, nor did he instruct Epstein to inform the Commission the statement was incorrect. His reason for doing nothing was that Epstein purportedly said that the incorrect information was inserted at Harris' suggestion. Caplin's purported reason for failing to advise the Commission of the correct facts is without substance.

Of utmost significance is Caplin's testimony as to Epstein's report to him following the meeting between Epstein, Harris and McQueeney. Harris reported he had furnished the staff with facts relating to Caplin's and Gotham's involvement in the Bolton matter. When asked what he was told by Epstein concerning immunity Caplin testified "Mr. Epstein said that it was

not within the legal power of the Commission to give me written immunity in the matter." He also testified that Epstein assured him that on the basis of his discussions with Harris the latter had authority "to commit the staff not to name Gotham and myself as respondents in the matter" and that he could waive his Fifth Amendment Privilege "with complete assurance that I would not be named in any administrative actions." In reviewing Caplin's entire testimony it is evident that Epstein never told Caplin he would receive "immunity" if he testified. Caplin admitted, when asked, that McQueeney never used the word "immunity" to him and the record shows Harris never used such word.

It is concluded that the staff informed Epstein that if Caplin testified it would not recommend inclusion of Caplin or Gotham as respondents in any administrative proceeding, that Epstein, as a result of his prior experience as a staff member, was well aware of the fact that staff recommendations are reviewed by higher levels of authority and that ultimately the Commission determined who would be named as respondents, that Epstein had been specifically advised by Harris that Borowski had ultimately authority to review any recommendations and that Epstein never stated he advised Caplin that Gotham or Caplin would receive immunity. It is further concluded that the only assurance Epstein received from the staff conducting the investigation was that it would not recommend that respondents be named in the proceeding. In fact, the staff conducting the investigation did not recommend that respondents be named, but the headquarters staff in Washington determined to include them

and Epstein was so advised. It is quite clear that Caplin drew conclusions from what his lawyer told him. If Caplin believed, prior to giving his investigative testimony, that he had immunity it may have been the result of either a failure of communication between Epstein and Caplin, or Epstein's failure to define precisely for Caplin's understanding the parameters of the staff's limited authority. Respondents have failed to demonstrate that any concrete promise had been made to Caplin that, if he testified, he would receive immunity. Nor, in light of Epstein's experience and knowledge of the Commission's practices and procedures regarding staff authority and levels of review, can it be concluded that he told Caplin that under no circumstances would he or Gotham be named as respondents if Caplin testified.

Other Matters

After Caplin testified as to his understanding of the events preceding his investigative testimony he refused to testify with respect to the issues set forth in the Order, particularly as to his conversations with Epstein regarding the involvement of Caplin and Gotham in the Bolton matter, claiming the due process provisions of the Fifth Amendment and the Administrative Procedures Act (APA). Notwithstanding a direction by the presiding Administrative Law Judge to answer such questions, Caplin persistently refused. The Division moved to strike all of his testimony upon the grounds that it was unfair to allow Caplin's testimony to remain without affording the Division the opportunity to cross examine as to conversations between Caplin and Epstein. Decision was reserved. The Division has renewed its request. The motion to strike will be denied. Though the opportunity

for cross-examination is a basic requirement in proceedings such as these[18/] such right was admittedly afforded with respect to Caplin's direct examination on the due process issue. Striking such testimony appears unwarranted. With respect to the issues involved in the order for proceeding it appears that if the Division believed such testimony was essential to the presentation of its case it could have pursued appropriate means to compel such testimony.

Respondents contend that since Caplin was available at the hearing his refusal to testify afforded no basis for admitting the tainted transcripts into evidence. In light of the analysis of respondents' contentions regarding lack of due process and fairness it is concluded that Caplin's transcripts are not tainted. Nevertheless, consideration is given to the question whether Caplin's investigative testimony was properly received in evidence. Such testimony is properly in evidence on two grounds. The Courts have consistently held that a party may introduce, as a part of his substantive proof, the deposition of his adversary and it is quite immaterial that the adversary is available to testify at the trial or has testified there. Community Counselling Service Inc. v. Reilly, 317 F. 2d 239, 243 (C.A. 4, 1963); accord Fey v. Walston & Co., Inc., 493 F. 2d 1036, 1046 (C.A. 7, 1974).[19/] Second, Caplin's transcripts are also

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18/ Siltronics, Inc., 41 SEC 658, 661 (1963).

19/ 4 Wigmore, EVIDENCE §1048-1049, 1052-1053 (1972); McCormick, EVIDENCE §262-263, 266 (2nd Ed. (1972)). The well-established rule that admissions of a party opponent is not hearsay has recently been adopted as Rule 801(d)(2)(A) of the Federal Rules of Evidence, effective July 1, 1975, P.L. 93-595, 88 Stat 1939, January 2, 1975.

admissable as declarations against his interest, since the testimony was contrary to his pecuniary and propriety interests and he rendered himself unavailable to testify at the hearing by invoking the Fifth Amendment.[20/] It is no moment, with respect to the admissability of the transcript, that Caplin did not plead the self-incriminatory provisions of the Fifth Amendment, but rather relied upon the due process provisions of the said amendment. Caplin's refusal to testify was premised on the privilege afforded by the Constitution by way of the said amendment. Just as the self-incriminatory provisions are a part of the Fifth Amendment, so too are the provisions relating to due process. In either case the privilege is available assuming the basis for the invocation of the privilege is present. In that connection it should be noted that in the instant case, the question is not one dealing with the propiety of the protection afforded by the Fifth Amendment, nor whether Caplin invoked the privilege in a proper manner or by the proper choice of words, manifested an intent to invoke his constitutional rights. The issue to be determined is whether in the light of Caplin's refusal to testify he became unavailable. It is concluded that since Caplin refused to testify and premised such refusal on a portion of the Fifth Amendment he became unavailable.[21/]

20/ 5 Wig ore, EVIDENCE §1455-1477 (1974); McCormick, EVIDENCE §276; Trade Development Bank v. Continental Ins. Co., 469 F.2d 35, 42 (C.A. 2, 1972); Vaccaro v. Alcoa Steamship Co., 405 F.2d 1133, 1137 (C.A. 2, 1968).

21/ The recently adopted Federal Rules of Evidence (See footnote 19 supra) defines "unavailability as a witness" to include situations where the declarant "persists in refusing to testify concerning the subject matter of his statement despite an order of the court to do so. Rules 804(a)(2) and (b)(1) and (3). See Rule 804(b)(5).

Public Interest

Having found that the respondents wilfully violated[22] or wilfully aided and abetted violations provisions of the Exchange Act and Rules thereunder, there remains for determination the question as to whether any sanction is appropriate in the public interest. Prior to such determination one matter should be noted. Respondents' defense during the course of the hearings related solely to their contentions of lack of due process and fairness.[23] The facts and circumstances relating to such contentions have been detailed earlier and need no repetition. Caplin's determination to rest his case solely upon such contentions resulted in his failure to refute both the testimonial evidence concerning the arrangements between Park and Gotham and the documentary evidence supporting such arrangements. Nevertheless, the sanctions imposed below are not premised upon Caplin's invocation of his alleged constitutional privilege nor upon his unproven claims of lack of due process. His right to assert such defenses is not questioned.

The facts, upon which the assessment is made regarding sanctions as to both respondents, demonstrate either Caplin's lack of understanding of the elements essential to the maintenance of a free and independent

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22/ It is well settled that "willful" in this context means intentionally committing the act which constitutes the violation. There is no requirement that the actor also be aware that he is violating a provision of the Act or the Rules thereunder. Tager v. SEC, 344 F. 2d 5 (C.A. 2, 1965).

23/ During the hearing respondents were afforded the same rights accorded to all parties including the opportunity to examine, cross-examine all witnesses, make objections to the testimonial and documentary material received in evidence and present their defenses.

market or a negligent disregard of activities engaged in by his brokerage firm, which activities at the very least, should have alerted him to the manipulative potential. With respect to Caplin's lack of understanding, the evidence shows that as chief executive officer of Gotham he gave Bergleitner approval to enter the sheets on Bolton and made no meaningful inquiry as to whether his employee had any information about the security or the issuer. His only concern was whether Gotham "could get hurt." An experienced and reliable broker-dealer should certainly understand that when he does not decide on his own initiative to make a market in the sheets, but is requested to insert quotations on the promise he would be protected on either side of the market the potential for manipulative conduct is present.

On the other hand assuming arguendo Caplin was not informed that Park would take Gotham's longs and supply his shorts, the record discloses that he checked Bergleitner's activities each evening and he knew or should have realized that Park was, in fact, at the other end of every Bolton transaction. That factor alone called for a searching inquiry particularly since the pattern of trading showed a consistent one eighth of a point profit. Such inquiry would have alerted Caplin not only as to the existence of the arrangements between Claridy and Bergleitner but that the latter was communicating with Claridy before accepting any order and that Claridy, in fact, was dictating the prices which Bergleitner was using.

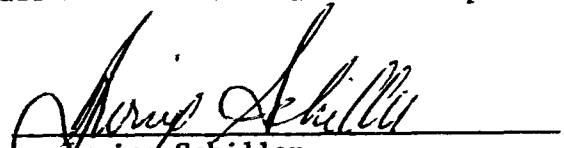
Considering the gravity of the violations found and the absence of mitigating factors it is concluded that the sanctions ordered below are appropriate in the public interest. Accordingly,

IT IS ORDERED that the registration of Gotham Securities Corp. as a broker-dealer is hereby revoked and that respondent Peter Caplin is hereby barred from association with a broker or dealer with the proviso that after a period of six months he may apply to become associated with a broker or dealer in a non-proprietary, non-supervisory capacity upon a satisfactory showing to the Commission that he will be adequately supervised.

IT IS FURTHER ORDERED that decision with respect to N. Carroll Mallow is hereby reserved pending future Commission determination.

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

Pursuant to Rule 17(f), this initial decision shall become the final decision of the Commission as to each party who has not, within fifteen (15) days after service of this initial decision upon him, filed a petition for review of this initial decision pursuant to Rule 17(b), unless the Commission pursuant to Rule 17(c) determines on its own initiative to review this initial decision as to him. If a party timely files a petition for review, or the Commission takes actions to review as to a party, the initial decision shall not become final with respect to that party. 24/



Irving Schiller
Administrative Law Judge

July 21, 1975
Washington, D.C.

24/ To the extent proposed findings and conclusions submitted by the parties, and the arguments made by them, are in accordance with the conclusions and views set forth herein they have been accepted, and to the extent they are inconsistent therewith they have been rejected.