ADMINISTRATIVE PROCEEDING
FILE NO. 3-7584

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of)
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THOMAS F. WHITE)
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INITIAL DECISION

Washington, D.C.
July 23, 1992

Warren E. Blair
Chief Administrative Law Judge

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APPEARANCES: Melvyn H. Rappaport and Lawrence S. Hing, of the San Francisco Branch Office of the Commission, for the Division of Enforcement.

Thomas F. White, pro se.

BEFORE: Warren E. Blair, Chief Administrative Law Judge

These public proceedings were instituted pursuant to Sections 15(b) and 19(h) of the Securities Exchange Act of 1934 ("Exchange Act") by order of the Commission dated September 27, 1991. The Order directed that a determination be made whether Thomas F. White ("White" or "respondent"), and Thomas F. White & Co., Inc. ("White & Co."), a registered broker-dealer, had, as alleged by the Division of Enforcement ("Division"), failed reasonably to supervise Steven M. Roberta ("Roberta"), a registered representative of White & Co., with a view toward preventing Roberta's violations of federal securities laws, 1/ and what, if any, remedial action would be appropriate in the public interest.

In substance, the Division alleged that during a period from February, 1986 through January, 1990 Roberta was subject to the supervision of White and that during that period White failed reasonably to supervise Roberta with a view to preventing Roberta's wilful violations of Section 17(a) of the Securities Act of 1933 ("1933 Act") and Section 10(b) of the Exchange Act, and Rule 10b-5 thereunder. 2/ The Division further alleged that Roberta's misconduct had resulted in his being found guilty of mail fraud, being permanently enjoined from violations of the antifraud provisions of the securities laws, and being barred from the securities business.

White's answer denied that Roberta had been subject to his supervision during the alleged period or that he had failed reasonably to supervise Roberta. White asserted as an affirmative defense that Roberta's misconduct could not have been detected by any amount of "procedural precaution."

As part of the post-hearing procedures, successive filings of proposed findings,

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1/ On March 12, 1992 the Commission issued its Findings and Order Imposing Remedial Sanctions against White & Co., Securities Exchange Act Release No. 30471, 50 SEC Docket 2159. Findings herein are binding only on White.

2/ Section 17(a) of the 1933 Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder are anti-fraud provisions in those Acts.

conclusions, and supporting briefs were specified. Timely filings were made by the parties.

The findings and conclusions herein are based upon the preponderance of the evidence as determined from the record and upon observation of the witnesses.

Respondent

White founded White & Co. in 1978 and the firm has been registered as a broker-dealer since that time. White was the firm's President and Chief Executive Officer ("CEO") until 1985 and is and since 1978 has been continuously Chairman of its Board of Directors. White relinquished the President and CEO positions in December, 1985 when he employed Joseph Baker ("Baker") to take over those positions. When Baker left White & Co. in January, 1989, White resumed his former positions of President and CEO. White is and has been the controlling stockholder of White & Co. since its inception.

White has been a registered representative for over twenty years and for the two years prior to forming White & Co. was employed by a securities firm as a branch manager. During the period from February, 1986 through January, 1990, White acted as White & Co.'s sales manager in charge of sales supervision and performed duties analogous to those commonly reposed in compliance officers in other securities firms.

VIOLATIONS OF ROBERTA

Roberta was hired by White as a registered representative in February, 1986, and became a vice-president at White & Co. in January, 1989. His employment with White & Co. was terminated for cause on January 23, 1990.

As alleged by the Division, the record establishes that Roberta pled guilty and on September 14, 1990 was convicted of mail fraud, in violation of Title 18, United States

Code, Section 1341. 3/ On August 14, 1991 Roberta was permanently enjoined by the United States District Court for the Northern District of California from fraudulently offering, selling, or purchasing securities 4/ as a result of a complaint filed against him by the Commission alleging that he had violated antifraud provisions of the Securities Act of 1933 ("1933 Act") and of the Securities Exchange Act of 1934 ("Exchange Act") 5/ On September 27, 1991 the Commission barred Roberta from association with any investment adviser, broker or dealer, investment company, or municipal securities dealer. 6/

Underlying each of those actions against Roberta is a fraud perpetrated upon White & Co. customers whose accounts were accessible to him. As part of his scheme Roberta made misrepresentations that induced customers to invest in a fictitious company which he named SRECOR, with an address that was in fact his own. In furtherance of his scheme Roberta set up a bank account in the name of SRECOR and used that account to deposit funds received from customers who intended to make investments in SRECOR. Roberta later converted the money in that account to his own use.

To persuade customers to agree to invest in SRECOR, Roberta on at least five occasions made different misrepresentations regarding SRECOR concerning the nature of its operations and the securities being offered. Among other misrepresentations he falsely represented that White & Co. was underwriting SRECOR's offering of securities which had

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3/ United States v. Roberta, CR-90-062-RHS (N.D. Cal. 1990).

4/ S.E.C. V. Steven M. Roberta, Civil Action No. C-91-2490-RFP (N.D. Cal. 1991).

5/ Section 17(a) of the 1933 Act, 15 U.S.C. §78j(b) and Rule 10b-5 thereunder, 17 CFR §240.10b-5.

6/ Steven M. Roberta, Securities Exchange Act Release No. 29744 (September 27, 1991), 49 SEC DKT 1636.

a definite maturity date with rates of interest which increased as the maturity date came closer, and that SRECOR was a fund that invested in high quality securities. After receiving customers' authority to invest in SRECOR, Roberta caused checks made payable to SRECOR to be issued by White & Co. against their accounts with the firm. Upon obtaining possession of those checks, Roberta deposited them in the SRECOR name bank account.

After receiving authority from customers to invest in SRECOR Roberta continued the fiction of SRECOR's existence in their minds by mailing to them fraudulent securities certificates purporting to represent their investments in SRECOR, forged confirmation slips and securities received slips on White & Co. forms purporting to confirm their purchases of SRECOR securities, and fictitious press releases about SRECOR.

By resorting to the described deceptions, Roberta succeeded during the period between February 1, 1989 and March 2, 1989 in having White &Co. issue nine checks payable to SRECOR in the total amount of $170,354.72.

It is clear from the record that Roberta engaged in fraud in connection with the offer and sale of SRECOR securities to White & Co. customers and that he used the mails to carry out that fraud. It is concluded that Roberta's misconduct constituted wilful violations of Section 17(a) of the 1933 Act, and of Section 10(b) of the Exchange Act, and Rule 10b-5 thereunder.

FAILURE OF WHITE TO SUPERVISE

The record having shown that Roberta committed the violations alleged by the Division while he was in the employ of White & Co., consideration must turn to the issue of whether White failed to exercise reasonable supervision over Roberta with a view to

preventing his violations. 7/ The Commission has frequently pointed out that the president of a brokerage firm is responsible for the firm's compliance with all applicable requirements unless and until he reasonably delegates a particular function to another person in the firm, and neither knows nor has reason to know that such person is not properly performing his duties. 8/ Here it appears obvious that White never made a reasonable or effective delegation of his authority with respect to the supervision of White & Co. registered representatives and that following the departure of Baker and White's resumption of the positions of president and CEO, White did not again make a reasonable or effective delegation of his authority over the operations and financial aspects of those operations of White & Co. It further appears that had White properly discharged his

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7/ Section 15(b)(4)(E) of the Exchange Act provides for the imposition of a sanction against a broker or dealer or a person associated with a broker or dealer who:

> ...has failed reasonably to supervise, with a view to preventing violations of such statutes, rules and regulations, another person who commits such a violation, if such other person is subject to his supervision. For the purpose of this subparagraph (E) no person shall be deemed to have failed reasonably to supervise any other person if --
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> (i) there have been established procedures, and a system for applying such procedures, which would reasonably be expected to prevent and detect, insofar as practicable, any such violation by such other person, and
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> (ii) such person has reasonably discharged the duties and obligations incumbent upon him by reason of such procedures and system without reasonable cause to believe that such procedures and system were not being complied with.

8/ Kirk A. Knapp, Securities Exchange Act Release No. 30391 (February 21, 1992), 50 SEC DKT 1840, 1845; Charles L. Campbell, Securities Exchange Act Release No. 26510 (February 1, 1989), SEC DKT 1391, 1395.

supervisory responsibilities, Roberta's violations might have been prevented.

White knew that compliance policies and procedures had to be adopted for governance of White & Co., but instead of writing a manual that met the needs of White & Co., White simply plagiarized the material in the White & Co. manual from other sources, including a major portion from the last securities firm where he had been a branch manager. The compliance manual in effect for use in White & Co.'s main office was devoid of procedures or policy statements regarding the duties of the office manager, cashier, or the margin clerk, nor was there provision for the handling of the receipt of securities and third-party checks. 9/

If White & Co. had adopted appropriate policies and procedures controlling the issuance of third-party checks to its registered representatives or if White had appropriately reviewed the firm's ledgers to determine the extent of the activity in the issuance of third-party checks and to whom those checks were being delivered, it is very possible that Roberta's scheme would have been thwarted at the outset or at least the extent of the fraud been limited.

Essential to the success of Roberta's fraudulent scheme and concomitant avoidance of early detection was White's abysmal lack of supervision over even the informal procedures regarding issuance of third-party checks adopted by the firm's back-office personnel in the absence of written directives. The unwritten procedures, based upon previous experience in the securities field, that the back office White & Co. personnel followed required the registered representative to submit a written check request to the margin clerk for approval. In the event that a customer requested a check payable to

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9/ "Effective supervision by broker-dealers is a critical element in the regulatory scheme. . . ." Mabon, Nugent & Co., 47 S.E.C. 862, 866 (1983).

anyone other than the customer against whose account it was to be drawn or deliverable to an address other than that shown on the customer's account, the margin clerk required a written letter of authorization signed by the customer to accompany the request. If the registered representative wanted to take possession of a check intended for a customer, the registered representative was required under unwritten policy to present a letter of authorization from the customer and to sign a ledger acknowledging personal receipt of the check.

But even these informal procedures were rendered ineffective by White's lack of supervision during the period starting February 1, 1989 when Roberta was able to persuade the margin clerk and the operations manager to process check requests and issue checks payable to SRECOR without the letters of authorization from the customers whose accounts were being charged. Roberta did sign the ledger, which was kept in the cashier's cage, on five occasions during the period from February 1, 1989 through March 14, 1989 indicating that five checks were received by him and against which accounts those checks were drawn payable to SRECOR. A review of the ledger would have alerted White to the unusually large dollar amount of third-party checks made payable to SRECOR and the identity of unsuitable investments by Roberta's customers, and would have indicated the extent of Roberta's involvement, but White never undertook to review the ledger to ascertain whether unusual activity was occurring.

White's failure to supervise and the absence of policies and procedures governing White & Co. registered representatives were additional factors that evidenced White's abdication of his responsibilities to attempt to prevent violations of the securities laws by White & Co.'s sales force. White failed to conduct compliance meetings with the registered representatives, made no provision for review of their incoming or outgoing mail to spot

questionable activities, and never undertook an independent review of Roberta's books and records to ascertain the identity and suitability of the investments Roberta was making for his customers.

In short, the record is replete with evidence that White from the inception of White & Co. gave obeisance to the concept of supervisory responsibilities and turned away from the discharge of his obligations in that area. His failures in that regard before, during, and after Roberta's fraud had been perpetrated ineluctably lead to the conclusion that White failed reasonably to supervise Roberta, a person subject to his supervision, with a view to preventing violations of the antifraud provisions of the securities laws.

White agrees that "Both Broker-Dealer and Broker-Dealer Supervisors are liable for Failure to Reasonable (sic) Supervise" 10/ but argues that "he, individually, adequately discharged his duty reasonably under the circumstances apparent at the time by delegating supervisory authority to others." 11/ White also agrees that "Proper Supervision Requires the Establishment of Procedures and Compliance with Such Procedures" 12/ and asserts that he responded immediately when first evidence of Roberta's violations came to his attention. White contends that Roberta's fraud was enabled by a lack of adherence of subordinate supervisors to White & Co. policies which were devised to "ensure compliance" with Commission regulations and to inattention of those employees to evidence of violations of White & Co. policies and procedures. The record does not support those arguments.

10/ White's Brief in Support of His Response to the Division's Findings of Fact and Conclusion of Law (hereafter referred to as "White's Brief"), at 15 (June 15, 1992).

11/ Id., at 17.

12/ Id., at 17

The Commission has long held that failure of supervision "connotes a failure to learn of improprieties when diligent application of supervisory procedures would have uncovered them." 13/ Here supervision by White as president, CEO, and sales manager, as well as that of White & Co. subordinate supervisors, with a view to preventing fraud such as that committed by Roberta was woefully inadequate. In particular, the record evidences an attempt by White to avoid supervisory responsibilities by employing and designating individuals to take responsibility for various segments of the firm's operations without White & Co. having adopted adequate supervisory procedures to guide its employees and absent clear directives from White concerning the authority of the subordinate supervisors. White hired Baker "to implement whatever was necessary to comply with all rules and regulations." 14/ However, during the relevant period and after the departure of Baker and the resumption by White of the positions of president and CEO of White & Co., the firm's Policies and Procedures manual was deficient with respect to back-office procedures. The fact that White employed personnel experienced in the areas of their responsibilities at White & Co. and that they continued to use procedures learned while in the employ of previous securities firms cannot excuse the absence of explicit directives regarding White & Co. policies and procedures enunciated by White. The weakness in White's defense is underlined by the failure of the unwritten procedure adopted in 1987 which required use of check request forms. When a customer requested that a check go to someone other than the customer, or to an address other than the address which appeared on the account, the practice of the margin clerk at White & Co. was to require something in writing from the

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13/ Blinder, Robinson & Co., Inc., 26 SEC DKT 238, 240 (1982).

14/ White's Brief, at 22.

client before issuance of the third-party check. It appears that the White & Co. operation manager felt free to ignore the third-party procedure and practice when a dispute arose between Roberta and the margin clerk when Roberta asked the margin clerk to process third-party check requests upon Roberta's verbal instructions. Had the unwritten procedures been honored instead of regarded as being flexible, it is clear that Roberta's scheme would have been to no avail.

Moreover, White cannot excuse his supervisory deficiencies with respect to the direct supervisory responsibility over Roberta and the other registered representatives of White & Co. As president of White & Co. and its sales manager, he failed reasonably to supervise Roberta with a view to preventing the violations Roberta committed. White argues that because he had no warnings concerning the problems that the back-office encountered with Roberta "or that the subordinate supervisors disregarded White & Co. policies and procedures," 15/ he was not in a position to take action against Roberta. But that argument assumes that White's supervisory responsibilities are discharged unless he has some warning regarding Roberta's derelictions. Section 15(b)(4)(E) is not to be so narrowly construed. That provision of the Exchange Act is an outgrowth of the 1963 Special Study of the Securities Markets which noted the need for greater supervision by broker-dealers over their salespersons and of the Commission's later request for greater authority to proceed directly against individuals for failure to supervise. 16/ The provisions of Section 15(b)(4)(E) require that supervisors reasonably supervise with a view to preventing the proscribed violations by the person under supervision. If, as here, reasonable

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15/ White's Brief, at 25.

16/ Arthur James Huff, Securities Exchange Act Release No. 29017 (March 28, 1991); 49 SEC DKT 878.

procedures to accomplish that purpose were not in place when the supervised person committed the violation, the absence of a warning regarding the onset of the misconduct is not a defense that can be accepted.

White argues that "it was reasonable for White to assume that his subordinate supervisors were aware of White & Co. policy given their training, work experience and background and Roberta had signed off on a document warning of the dangers of 'selling away,'" 17/ and further that it is not imperative that policies and established procedures be in writing. While it may be true that all policies and procedures need not be in writing, it is vital that they be known to subordinate supervisors and implemented. The record does not support White's assumption that it was reasonable for him to assume those subordinates were aware of White & Co.'s policies and procedures, but to the contrary reflects considerable confusion in the minds of the supervisors responsible for various aspects of the firm's sales and back-office operations concerning their duties and responsibilities. Even if White's assumption were accepted, he would not have discharged his responsibilities as president and CEO of White & Co. to implement and assure compliance with rules and regulations applicable to White & Co. The Commission has in no uncertain terms set the standards expected of broker-dealers, saying:

> Apart from adopting effective procedures broker-dealers must provide effective staffing, sufficient resources and a system of follow up and review to determine that any responsibility to supervise delegated to compliance officers, branch managers and other personnel is being diligently exercised. 18/

Not only were the written and unwritten policies and procedures of White & Co. seriously deficient, but there were no effective measures to assure compliance in existence

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17/ White's Brief, at 22.

18/ Mabon, Nugent & Co., supra.

during the relevant period. Linda Frodesen, the person named as compliance officer, testified, and her testimony is credited, that she worked with White & Co. as a discount broker for the three and a half years from May 1982 to around 1986, went with another securities firm as a sales assistant for ten months, and was rehired as a sales assistant to White in June, 1987. After assisting White for a short while, she assisted Baker as general office manager and held that position until again leaving White & Co. in May, 1990. According to her, most of her duties involved taking care of personnel records, helping out in the trading room when someone was absent, and assuring that the office generally ran smoothly. In speaking of her, White referred to her as "chief cook and bottle washer," 19/ but her testimony specifically negates any involvement in disputes regarding third-party checks and limits her compliance duties to minor matters such as approving new account forms and reviewing incoming mail for complaints which, if minor, were taken care of by her or, if more serious, by Baker or Michel Millette, Senior Vice President - Chief Financial Officer. Major problems would be referred to White. It is clear from the record that although Frodesen carried the title of Compliance Officer, she in fact did not in any significant or effective manner carry out the duties normally expected of a person acting in that capacity in a securities firm, and was not charged by White to carry out duties normally given to compliance officers in other securities firms.

White further claims that compliance matters were also taken under consideration by a Compliance Committee whose members initially were White, Baker, and Millette. After Baker's departure, White, according to his testimony, added Frodesen and Roger

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19/ Tr. 116.

Sheridan, White & Co.'s operations manager, to the Compliance Committee. 20/ However, the record discloses that the Compliance Committee was in fact nothing more than a committee in name only. It did not have scheduled meetings and no minutes were taken of informal meetings nor a record made of the matters discussed. The reality of the Compliance Committee was well depicted by White when he testified:

> Q. Between 1985 and 1988, December 31.
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> A. Our Compliance Committee -- when two people are on the run, I mean we discuss a problem perhaps walking down the hall. That's our Compliance Committee. And they'll say, "John O'Connor has a customer that says that he didn't get -- has a problem of some sort and what are we going to do about this problem?" And that -- and so that is -- that was our -- we had two or three people involved in a decision that affected compliance.
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> Q. So it was a majority vote of the Compliance Committee if only two of you were walking down the hall, the meeting was held, you discussed it, and then the verdict was rendered, is that it? Is that correct?
>
> A. Yes. 21/

In brief, the record establishes that White assumed and did not effectively or adequately delegate his supervisory responsibilities over the activities of the firm's sales representatives nor the activities and duties of the other employees. Compliance was obviously a secondary consideration for White who claimed expertise only in the sales area and who obviously lacked interest in putting controls in place that could have prevented the violations committed by Roberta. Most telling regarding the insufficiency of White's supervision and the firm's compliance practices and procedures is the fact, as the Division highlighted in its argument, that Roberta's blatant fraud was not uncovered by White until

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20/ When asked by the Division, "After Mr. Baker left, were you a member of the Compliance Committee, sir?", Sheridan answered, "Not that I recall, no." Tr. 444.

21/ Tr., at 345.

January, 1990, almost a year after Roberta fraudulently obtained the first of the White & Co. checks in carrying out his scheme. 22/

PUBLIC INTEREST

Having determined that White failed reasonably to supervise with a view to preventing Roberta's violations of Section 17(a) of the 1933 Act and of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, it is necessary to consider the remedial action appropriate in the public interest because of his supervisory derelictions.

The Division submits that it is in the public interest that White be suspended from being associated with a regulatory entity in a supervisory capacity for a period of twelve months. In support of its recommendation, the Division not only points to Roberta's misconduct, which reasonable supervision by White might have averted, but calls attention to the long-continuing deficiencies in White's supervisory practices from the inception of White & Co., and to the history of sanctions imposed by the National Association of Securities Dealers, Inc. ("NASD") upon White and his firm. In that regard, the record evidences that in October, 1983, the NASD censured and fined White & Co. and White $1,500 for seven violations of the NASD's Rules of Fair Practice relating to operational practices of White & Co. Another NASD action resulted in White and White & Co. being censured and fined $3,000 in May, 1985, for failure to supervise the activities of Jack Teeters, a registered representative. The NASD also found it necessary to send White and White & Co. a "letter of caution" on May 15, 1990 regarding, among other matters, the deficiencies in the firm's supervisory procedures including the failure of their written procedures to specifically assign, by name, each registered person to a supervisor, and to

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22/ Brief of the Division of Enforcement, at 16 (March 6, 1992).

designate appropriately qualified principals to carry out White & Co.'s supervisory obligations with respect to each type of business it engaged in.

White brushes aside the NASD disciplinary actions in 1983 as involving technical violations which he decided "it was best to get it over by accepting the censure and fine" 23/ and asserts "In retrospect, White should have appealed." 24/ Apparently White considered the NASD action as de minimis in nature and felt that he had no need to improve the practice and procedures of White & Co. With respect to the NASD censure and fine of $3,000 against White and White & Co. in May, 1985 for failure to reasonably supervise the activities of one of the firm's registered representatives, White's response is that "It was an honest mistake and White accepted the censure and small fine. The lesson White learned was not to rely on attorneys." 25/ Noteworthy is the fact that it did not occur to White at the time of that NASD action nor since that he was put on notice that he should be taking his supervisory responsibilities more seriously. In any event, the NASD's concerns with White and his firm did little, if anything, to trigger remedial action by White to improve his supervisory practices and procedures. White argues further that two censures and small fines for technical violations in 29 years in the business are "not a cause for concern of the public interest and White feels these should have no bearing on the present case." 26/ In his view, "No sanctions are appropriate, much less a

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23/ White's Response to the Division's Proposed Findings of Facts & White's Proposed Findings of Facts, at 25 (June 15, 1992).

24/ Id.

25/ Id., at 26.

26/ White's Brief, at 14.

suspension." 27/ But the Commission has long viewed previous disciplinary actions against a respondent in an entirely different light than that advocated by White, and as matters to be taken into consideration in determining appropriate remedial action against a respondent. 28/

Upon careful consideration of the record, the arguments and contentions of the parties, and the previous disciplinary actions against White and White & Co., it is concluded that in the public interest White should be suspended from association in a supervisory position with any broker or dealer for a period of twelve months. Although the sanction may seem harsh to White, his previous inability to recognize his supervisory shortcomings, which contributed to still further failures to reasonably supervise as recorded in these proceedings, demands imposition of stern remedial action. The imposition of a twelve-month suspension may serve to impress upon White the seriousness with which the Commission views supervisory responsibilities of those assuming oversight of compliance practices and procedures within a securities firm and serve to deter compliance personnel with other securities firms from taking their supervisory responsibilities lightly. 29/

ORDER

IT IS ORDERED that Thomas F. White is suspended from acting in a supervisory capacity with any broker or dealer for a period of one year.

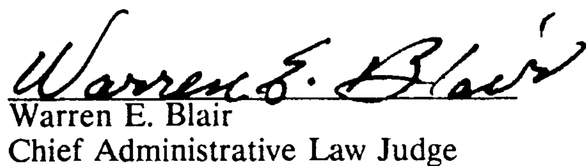
27/ Id.

28/ See e.g. Goffe-Carkener-Blackford Securities Corp., 45 S.E.C. 975, 980 (1975).

29/ All proposed findings and conclusions submitted by the parties have been considered, as have their contentions. To the extent such proposals and contentions are consistent with this initial decision, they are accepted.

This order shall become effective in accordance with and subject to the provisions of Rule 17(f) of the Rules of Practice.

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



Warren E. Blair
Chief Administrative Law Judge

Washington, D.C.
July 23, 1992