ADMINISTRATIVE PROCEEDING
FILE NO. 3-3460

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of

BLACK & COMPANY, INC.
LAWRENCE S. BLACK
ROY A. PITT, JR.
R.W. PRESSPRICH & CO., INC.

INITIAL DECISION

July 12, 1974
Washington, D.C.

David J. Markun
Administrative Law Judge

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APPEARANCES: Lane B. Emory, Assistant Administrator, Seattle Regional Office, and Gary A. Swenson, attorneys for the Division of Enforcement.
Barnes H. Ellis, of Davies, Biggs, Strayer, Stoel and Boley, Portland, Oregon, for Respondents Black & Company, Inc. and Lawrence S. Black.
Wallace Aiken and Gerald L. Bopp, of Aiken, St. Louis & Siljeg, Seattle, Washington, for Respondent Roy A. Pitt, Jr.
A. Edward Grashof, of Winthrop, Stimson, Putnam & Roberts, 40 Wall Street, New York, N.Y., for Respondent R.W. Pressprich & Co., Inc.

BEFORE: David J. Markun, Administrative Law Judge

THE PROCEEDING

This proceeding[1/] was instituted by an order of the Commission dated December 21, 1971 ("Order"),[2/] pursuant to Sections 15(b), 15A and 19(a)(3) of the Securities Exchange Act of 1934 and Section 203(e) of the Investment Advisors Act of 1940 against six corporate and six individual respondents[3/] to determine whether respondents wilfully violated or wilfully aided and abetted violations of the antifraud provisions of Section 17(a) of the Securities Act of 1933 ("Securities Act"), Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act")

1/ The Commission made the proceeding, initially designated private, a public proceeding by its order of January 16, 1973, at the request of the Seattle Post Intelligencer, in view of the substantial interest of the people of the State of Washington in the proceeding.

2/ The Order was amended by the Commission by order of October 20, 1972, to add charges of failing reasonably to supervise against the broker-dealer respondents, and was further amended at the outset of the hearing for technical reasons by stipulation of the parties approved by the Administrative Law Judge on January 8, 1973 (see Exhibit ALJ No. 1). A compilation of the original Order as modified by these two amendments appears as Exhibit ALJ No. 2.

3/ This initial decision has application only to the four respondents named in the caption, the other respondents having made settlements with the Commission (see Commission releases 34-9921; 34-9979; 34-10120; 34-10406). However, since the violations respecting Respondent Pitt involve respondents who have settled out, there will necessarily be some mention of such respondents in this decision.

and Rule 10b-5 thereunder,[4] and of Section 206(4) of the Investment Advisors Act of 1940 ("Advisors Act") and Rule 206(4)-1 thereunder,[5] whether they committed various alleged,related record-keeping violations, whether certain respondents failed reasonably to supervise, and the remedial action, if any, that might be appropriate in the public interest. The charges arise out of an allegedly fraudulent and deceitful practice under which Respondent broker-dealers and their agents during the period from about September 1965 to about October 1969 (the "relevant period") allocated to Respondent Roy A. Pitt, Jr. ("Pitt"), then Executive Secretary of the State Finance Committee of the State of Washington ("SFC"), "hot" new issues of stock and gave him other "substantial benefits" in connection with the receipt by such broker-dealer respondents of "substantial business" in the form of securities transactions transacted through them by Pitt on behalf of various funds administered for agencies of the State of Washington by the SFC.

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4 / 15 USC 77q(a); 15 USC 78j(b); 17 CFR 240.10b-5. Rule 10b-5 provides as follows:

> Rule 10b-5. Employment of Manipulative and Deceptive Devices. It shall be unlawful for any person, directly or indirectly, by use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange
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> (1) to employ any device, scheme, or artifice to defraud,
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> (2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
>
> in connection with the purchase or sale of any security.

5 / Division counsel during the course of the hearing indicated it would present no evidence in support of the charges of violations of Section 206(4) of the Investment Advisors Act or of Rule 206(4)-1 thereunder, thereby, in effect, abandoning such charges; there being no evidence in the record to support findings of violations of such provisions those charges are hereby dismissed.

This initial decision has application only to the four respondents named in the caption, the other respondents having made settlements.[6/]

The evidentiary hearing was held in Seattle, Washington, from January 8 to January 19, 1973. All parties have been represented by counsel throughout the proceeding.

The parties have filed proposed findings of fact, conclusions of law, and supporting briefs[7/] pursuant to Rule 16 of the Commission's Rules of Practice, 17 CFR 201.16. Because of the novelty and complexity of the issues presented, oral argument was ordered and held on April 18, 1974, in Seattle, Washington, on motion of Respondents Black & Company, Inc. and Lawrence S. Black.

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

FINDINGS OF FACT AND LAW

The Respondents

Respondent Roy A. Pitt, Jr. ("Pitt"), 48, took up employment in the securities industry in 1941 and except for an interruption of about 2 years for military service during World War II was continuously employed in the industry until October, 1960. During those years Pitt

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6/ See footnote 3 above.

7/ Respondents Black & Company, Inc. and Lawrence S. Black filed a reply brief dated 3-15-74 to the Division's reply brief and Respondent R.W. Pressprich & Co., Inc. filed a 4 page letter dated 3-14-74 in lieu of a reply brief. While neither the March 15th reply brief nor the March 14th letter was called for under the briefing schedule established at the post-hearing procedures, the arguments and points made in both have been given full consideration.

acquired extensive experience respecting corporate and municipal bond transactions, including experience as branch manager of a broker-dealer firm that dealt primarily in the purchase and sale of such securities.

In October of 1960 Pitt was appointed Executive Secretary of the State Finance Committee of the State of Washington ("SFC"). The SFC is a committee established under laws of the State of Washington to provide supervision over the investment and management of monies belonging to a dozen or more state funds ("the funds"), e.g. the Teachers Retirement Fund and the State Patrol Retirement Fund. The monies of the funds were invested in various securities, principally corporate, government and municipal debt securities.[8/]

During the relevant period (September, 1965 through October, 1969) the membership of the SFC comprised the Governor, the Lt. Governor, and the State Treasurer, the last of whom served ex officio as chairman. The SFC met infrequently and left the day to day operations of the SFC and supervision of its small staff in Olympia, Washington, to Pitt.

It is uncontested, and the record establishes, that during the relevant period Pitt had absolute discretion (subject to state law specifying the classes of securities that could be purchased for the funds) to decide what purchases and sales of securities to make for the funds, the amount of and timing of such purchases and sales, and the broker-dealer through whom he would execute transactions on behalf of the SFC.[9/]

8/ Within the relevant period statutory changes respecting some of the funds authorized investment in a broader range of securities, thus enabling the SFC and Pitt to endeavor to increase the investment yield for such funds.

9/ It was Pitt's general practice to personally decide what securities to purchase or sell for the funds and to personally place the orders with the various broker-dealers with whom he dealt, although on occasion he would delegate follow-up details to his assistant, Charlotte Wheat.

During the relevant period Pitt made annual purchases and sales of securities in the range of some $742 million to $1 billion for the SFC, and by the end of the period the total current book value of the investments administered by Pitt and the SFC for the funds had come to exceed $1 billion. Since the SFC account was a major institutional account in the Pacific Northwest, Pitt had numerous contacts, both in person and by phone, with representatives of numerous broker-dealers competing vigorously to do business with the SFC.

In August of 1969 Pitt resigned his position as Executive Secretary of the SFC after becoming the subject of intensely adverse newsmedia publicity concerning his purported personal securities transactions and other matters during the relevant period. It appears that this public inquiry was triggered by the complaints of local Washington State broker-dealers who objected to the volume of SFC transactions that was going to out-of-state broker dealers.

Respondent Black and Company, Inc. ("Black Company") is a broker-dealer with principal offices in Portland, Oregon,[10/] that has been registered as a broker-dealer with the Commission since 1959. It is a member of the New York Stock Exchange ("NYSE") and other national stock exchanges[11/] and of the National Association of Securities Dealers, Inc. ("NASD"). During the relevant period Black Company employed approximately 50 to 150 persons and generated gross income of from $1 to $5 million annually. Black Company is the only Oregon-headquartered

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10/ During all or portions of the relevant period Black Company also had offices in New York and San Francisco and a research unit in Philadelphia

11/ During all or portions of the relevant period Black Company was an associate member of the American Stock Exchange and a member of the Pacific Coast and Midwest Stock Exchanges.

NYSE member firm and of all Oregon-headquartered firms it has the highest volume of corporate financings and underwritings.

During the relevant period the SFC made total securities purchases of somewhat over $1,600,000 from Black Company, on which the firm realized approximately $10,000 in gross commissions.

Respondent Lawrence S. Black ("Black") has been in the securities industry for over 22 years, commencing in 1952 with Foster & Marshall, a NYSE member, then with Dominick & Dominick in New York, N.Y. during 1954-1957, and later, from 1957 to 1959, as manager of the bond department of Foster and Marshall in Portland, Oregon, before founding Black Company in 1959. Black continued to own over 50% of the stock of Black Company and to act as its president and chief executive officer through 1969.

The business Pitt did with Black Company during the relevant period on behalf of SFC was done exclusively through Black, who was fully aware throughout this period of Pitt's official position, responsibilities, and authority.

R.W. Pressprich & Co., Inc. ("Pressprich") is a corporation which has been registered with the Commission as a broker-dealer since April 26, 1968. Its principal offices are in New York, N.Y., and it has a branch office in Portland, Oregon, which figures in the transactions involved in this proceeding. Pressprich, as a corporation, succeeded on March 1, 1968 to the business of R.W. Pressprich & Co. ("Pressprich"),[12/] a partnership, which had been registered as a broker-

12/ The corporation and the partnership are both referred to herein as "Pressprich", and the particular entity to which reference is made will depend upon the date or time involved.

dealer with the Commission from September 21, 1940 to October 25, 1970. The stockholders, directors, and principal officers of the Pressprich corporation upon its formation were to a substantial extent persons who were general partners of the Pressprich partnership. Pressprich is a member of the NASD, the NYSE, and other national securities exchanges.

During the relevant period Pitt, on behalf of SFC, had purchase and sale transactions with Pressprich totalling somewhat over $17,740,000. During that period the SFC was one of the larger accounts in Pressprich's Portland office.

Violations by Pitt

The thrust of the allegations against Pitt is that during the relevant period (September 1965 through about October, 1969) Pitt, by use of jurisdictional means, engaged in various acts, practices, and a course of conduct that violated the antifraud provisions of Section 17(a) of the Securities Act and of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder (1) by his acceptance of "substantial benefits" for his personal use and benefit from six respondent broker-dealers or their representatives, which broker-dealers during that period were given substantial SFC business[13/] by Pitt and (2) by his failure to disclose to

13/ Besides Black Company and Pressprich, the amounts of whose official business with SFC have already been stated above, the four broker-dealer firms who have made settlements with the Commission in this proceeding transacted securities business with the SFC during the relevant period in the following amounts: over $3,600,000; over $4,000,000; over $17,000,000; and over $80,500,000. It is concluded that all of these amounts, including those for Black Company and Pressprich, represented "substantial" amounts of securities purchase and sale transactions by SFC with the broker-dealer firms within the meaning of the allegation in the Order.

During the relevant period Pitt dealt with an estimated 200 to 250 salesmen representing some 75 to 90 broker-dealer firms in connection with SFC business.

SFC as representatives of the beneficiary owners of the Funds administered by SFC the fact that he was receiving for his personal use and benefit such "substantial benefits".

The record establishes that during the relevant period while managing fund portfolios for the SFC Pitt engaged in the purchase and sale of securities for his own benefit through a checking account at the Seattle Trust and Savings Bank ("Seattle Trust" or "the Bank"). The checking account was in the name of his wife, Jeanne M. Pitt,[14/] but it is undisputed that all securities transactions conducted through the account were ordered and directed not by his wife but by Pitt.[15/] By September, 1965, Pitt had arranged a procedure with officers of Seattle Trust under which Pitt would order a new issue of a security through a representative of a broker-dealer and have such firm[16/][17/] charge the transaction

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14/ There appears to be some confusion in the Seattle Trust records as to the designation of the account. For a given period the customer's ledger lists both Pitt and his wife, for another period only Mrs. Pitt, and for still another period only Pitt. This confusion probably resulted from the fact that although the account was formally that of Mrs. Pitt the bank's directions respecting transactions therein came only from Pitt and confirmations and statements relative to the account were mailed to Pitt in care of the SFC.

15/ Pitt regarded both himself and his wife as beneficial owners of the account on the basis that Washington is a community-property state. Since Pitt had de facto control of the account and at least part ownership therein, the account is treated herein as his account.

16/ With only one exception, all stocks purchased by Pitt in the described manner were new issues.

17/ The broker-dealers from whom Pitt purchased securities through Seattle Trust included five of the six broker-dealers named as respondents in this proceeding and two broker dealers, from whom single purchases were made, who were not so named.

to an account carried in the name of Seattle Trust, and confirm the purchase of the security and deliver the security to Seattle Trust without disclosing on the confirmation that the purchase was for Pitt.

As a general practice, after Pitt ordered the purchase of a new issue from a broker-dealer he would telephone the officers of Seattle Trust[18/] to advise them he had done so and that the confirmation and the security from the broker-dealer would be arriving at Seattle Trust in due course, after which the Bank, in accordance with pre-established understandings, would receive the broker-dealer's confirmation, accept delivery of the stock and pay for it when received, and thereafter debit Pitt's checking or loan account[19/] for the purchase price.[20/]

When Pitt desired to sell a security he had thus purchased through the Seattle Trust account he would call the Bank and instruct its officers or employees to sell the security. The Bank would exercise its own discretion in choosing a broker-dealer through which the security would be sold, and in no instance was any one of Pitt's securities sold through the broker-dealer from whom he had purchased it. At the time Pitt would give Seattle Trust personnel "sell" instructions he would

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18/ The officer or officers he dealt with at the Bank were not trust department officers but investment-department officers with whom he transacted official business on behalf of the SFC. Pitt's was the only individual account that was handled by the Investment Department of the Bank.

19/ In March of 1969 Pitt obtained a line-of-credit from Seattle Trust in the amount of $15,000 to use in the financing of securities purchases. Interest was paid by Pitt to the extent that the line of credit was drawn upon. The line-of-credit "loan" was secured by the deposit of securities.

20/ In the numerous cases in which Pitt gave the Bank instructions to sell the stock in the same converstation in which he advised them he had purchased it, or a day or so later, it appears that the Bank deferred debiting and crediting Pitt's account until the stock was received from the selling broker and, presumably the same day, delivered out to the broker-dealer who had purchased from Pitt.

generally tell them what price he expected it would sell for and what, in his view, the market conditions were. On a number of occasions Pitt instructed Seattle Trust personnel to sell the security in the same conversation in which he advised them that the security had been purchased and would be arriving from a particular broker-dealer.

The arrangement Pitt had with Seattle Trust was of benefit to Pitt in terms of financing his purchases of new issues since he was thus able to take advantage of the fact that the Bank was not required to pay for the securities until they were actually delivered to the Bank, whereas Pitt as an individual would have had to pay for the stock within 7 days of the time he purchased it.[21/] This factor was of particular significance as respects new issues since there is frequently a considerable delay before the new issue is delivered, because frequently larger stock certificates must be broken-down into certificates reflecting the numbers' of shares purchased by individual purchasers. Thus, as to those new issues that Pitt sold when he purchased them or at any time before the shares he purchased were delivered to the Bank, he was able to realize a profit without ever having advanced any of his own funds.

During the relevant period Pitt made 24 purchases and related sales[22/] of securities through his account at Seattle Trust. All of these purchases (usually not over 100 shares), with the exception of Hillhaven, Inc., were purchases of new issues. Of the 23 new issues, Pitt sold 5

21/ Additional benefits resulting to Pitt from handling these transactions through Seattle Trust were the lack of any service charge, (limited) free-overdraft privileges, lack of any commission charge by the Bank on the transactions, and ease of handling.

22/ One security was sold otherwise than through Seattle Trust.

on the same day they were purchased or the next day[23/] and sold an additional 8 issues within 14 days of the respective dates of purchase.[24/]

Pitt's total purchases of new issues through Seattle Trust during the relevant period totaled approximately $47,000, on which he realized a profit in excess of $8,000, with each issue showing a substantial profit except a 1969 purchase of Integrated Containers, on which Pitt lost $1,293.75 after holding the stock 224 days.

After Pitt resigned as Executive Secretary of the SFC in August, 1969, his line-of-credit loan account at Seattle Trust was closed out and Pitt thereafter purchased no additional new issues of stock.[25/]

During the relevant period, in May, 1967, Pitt also purchased 427 shares of Hillhaven (not a new issue) at a reduced price of $5 per share from one of the broker-dealers who has settled-out in this proceeding, and from whom Pitt purchased no other stock. On the same day he bought Hillhaven, Pitt sold 150 of the shares at $14.50, thus realizing enough to finance the purchase of the entire 427 shares, and a year later sold the remaining 277 shares at $32.00 a share for additional gain. From the president of this same broker-dealer Pitt also received a $1,000 fee for the preparation of a 3 page list of institutional investors in the Midwest familiar to Pitt. The data contained in the list were available from other published sources

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23/ It seems probable that securities sold on the next day were actually ordered to be sold by Pitt on the same day the securities were delivered to the Bank and that there was simply a delay in executing the sale.

24/ While these figures include purchases from Black Company and Pressprich, more specific and detailed findings will be made below regarding these respondents in sections of this decision treating their involvement.

25/ Apart from brief employment with Black Company to assist them with a short-range matter, Pitt was not successful in getting employment in the securities industry after leaving the SFC.

and the $1000 fee was far in excess of its true worth.

From still another broker-dealer who settled out in this proceeding Pitt purchased no new issues, but did accept gifts and gratuities in various forms. In February, 1968, the resident partner of the San Francisco Office of this New York broker dealer ("resident partner") loaned $400 to Pitt to enable him to maintain the required amount of collateral in his margin account at the San Francisco office of this broker dealer. Pitt was not required to repay this loan in full.[26/] On July 9, 1968 the resident partner gave Pitt a check for $100 for a purpose she could not later clearly recall and on November 18, 1968, she again "loaned" Pitt $500 which she did not require him to repay. From November 30 to December 5, 1968, Pitt attended the Investment Bankers Association ("IBA") Convention in Miami, Florida, this broker-dealer having paid his round-trip air fare and also his hotel expenses, though the broker dealer had never previously paid similar expenses for anyone in Pitt's general situation.

The United States mails and interstate telephone systems were utilized extensively by Pitt and others concerned in transacting the SFC securities business with the broker-dealers named as respondents in this proceeding, and such facilities were also employed in connection with the securities transactions mentioned above that were for Pitt's personal use and benefit.

During all or substantially all of the relevant period Pitt, as an officer and official of the State of Washington, was subject to the provisions of Chapters 21 and 22 of Title 42 of the Revised Code of

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26/ Either $150 or $250 of this loan was repaid, but no part of the subsequent "loans" was repaid.

Washington (42.21.010-42.21.090; 42.22.010-42.22.120). For convenience, these provisions, in the annotated form, are attached hereto as Appendix A. 27/

Section 42.21.010 of the Revised Code of Washington states the "Declaration of necessity and purpose" of title 42, Chapter 21 entitled "CODE OF ETHICS FOR PUBLIC OFFICIALS", and Section 42.21.030 sets forth certain "Prohibited Practices", in the following terms:

> 42.21.010 Declaration of necessity and purpose. It is declared that high moral and ethical standards among public officials are essential to the conduct of free government; that a code of ethics for the guidance of public officials is necessary to prevent conflicts of interest in public office, improve standards of public service, and promote and strengthen the faith and confidence of the people of the state of Washington in their public officials.
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> LEGISLATIVE HISTORY
> Enacted Laws 1st Ex Sess 1965 ch 150 § 1 p 224.
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> * * *
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> 42.21.030 Prohibited practices--Using position to secure special privileges or exemptions. No public official shall use his position to secure special privileges or exemptions for himself, his spouse, child, parents or other persons standing in the first degree of relationship.
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> LEGISLATIVE HISTORY
> Enacted Laws 1st Ex Sess 1965 ch 150 § 3 p 2245.

In similar vein, Sections 42.22.010, 42.22.030 and 42.22.040 of Title 42, Chapter 22, entitled "CODE OF ETHICS FOR PUBLIC OFFICERS AND

27/ The Division also contends that paragraph (1) of Section 42.20.010, also set forth in Appendix A, applied to Pitt's conduct as charged in this proceeding. It is concluded that this contention is not well founded for the reason that Pitt did not accept a gratuity or reward "for omitting or deferring the performance of any official duty" (emphasis added) but rather in connection with performing such official duty.

EMPLOYEES", provide in pertinent part as follows:

42.22.010 Declaration of necessity and purpose. It is declared that the high moral and ethical standards among the public servants are essential to the conduct of free government; that a code of ethics for the guidance of public officers and employees is necessary in order to eliminate conflicts of interest in public office, improve standards of public service, and promote and strengthen the faith and confidence of the people of Washington in their government.

LEGISLATIVE HISTORY
Enacted Laws 1959 ch 320 § 1 p 1555.

* * *

42.22.030 Activities in conflict with discharge of duties prohibited. No officer or employee of a state agency or legislative employee shall have any interest, financial or otherwise, direct or indirect, or shall engage in any business or transaction or professional activity, or shall incur any obligation of any nature, which is in conflict with the proper discharge of his duties in the public interest.

* * *

42.22.040 Prohibited practices enumerated—Agency code of ethics. No officer or employee of a state agency, legislative employee, or other public officer shall use his position to secure special privileges or exemptions for himself or others.

* * *

(2) No officer or employee of a state agency, or other public officer shall, directly or indirectly, give or receive or agree to receive any compensation, gift, reward, or gratuity from any source except the state of Washington, its political subdivisions, or employing municipal government, for any matter connected with or related to his services as such an officer or employee unless otherwise provided for by law.

Pitt was subject to the provisions of the Codes of Ethics prescribed by Title 42, Chapters 21 and 22, of the Revised Code of Washington. In 1967 and 1969 he filed with the Secretary of State the written statement required of public officials under Section 42.21.060 concerning specified private interests.[28/]

Acceptance by Pitt of the unrepaid "loans" was in clear violation[29/] of these statutory provisions, since the record as a whole makes it clear that the "loans"were extended to Pitt because of his status as Executive Secretary to the SFC and in connection with the SFC's doing of business with the particular broker-dealer.[30/] Testimony that the "loans" were prompted by friendship is not credited; in any event, even if believed, such fact would be irrelevant since the Washington State statutes flatly prohibit acceptance of such a gift or favor by a man in Pitt's position in these circumstances.

Acceptance by Pitt of the air fare and hotel expenses in connection with his attendance at a meeting of the IBA in Miami, Florida, presents a closer question since as to that the record shows that at least one

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28/ Pitt filed no statement in 1968 because, he testified, he had or held nothing that had to be declared that year. Parenthetically, the statement required by this provision would not call for Pitt's disclosure of his receipt of "hot" new issues or of gifts in the form of "loans" not expected to be repaid, or of the "discounted price paid in his purchase of Hillhaven stock.

29/ See note 77 below.

30/ The same is true of his "discounted" purchase of Hillhaven stock and his receipt of $1,000 for a list of broker-dealers that was in fact worth much less.

member of the SFC, the State Treasurer, was aware that such expenses were being paid for Pitt by the broker-dealer, and more importantly, it would appear that the benefits of attendance at such meeting inured primarily to the SFC rather than to Pitt. As the State Treasurer testified, the SFC would probably have approved and paid for Pitt's attendance at such a meeting, and, indeed, Pitt could have authorized his own travel expenses in connection therewith. In view of these factors, it is concluded that acceptance by Pitt of the Miami-Trip expenses is not established as violative of the statutory code-of-ethics provisions nor of the antifraud provisions of the Securities Act and the Exchange Act.

On the other hand, acceptance by Pitt of allocations of new issues, at least to the extent that they involved "hot" issues, clearly violated the statutory codes-of-ethics. A "hot issue" is generally understood in the industry to refer to a new issue of a security that immediately or rapidly rises to a premium after it becomes available for trading in the secondary market.[31/] Hot issues rise to a premium because they have been oversubscribed, i.e. interest in the issue exceeded the available supply of the stock. From the expressions of interest in the stock before registration of it becomes effective, it is possible for the broker-dealers participating in the distribution of the new issue to predict with considerable accuracy whether the new issue will become a "hot" stock, or, in the language of the Order, whether the stock could

31/ See Report of the Special Study of the Securities and Exchange Commission, H.R. Doc. No. 95, Pt. 1, 88th Cong., 1st Sess. pp. 514-518 (1963).

be allocated or purchased ". . . with the expectation that the price would rise to a premium subsequent to the effective date of the offerings . . . ."

Of the 23 new issues purchased by Pitt during the relevant period at least 17 are established by the record as having been hot issues.[32/] In 13 of the 17 hot issues, Pitt either did realize, or could have realized, a substantial profit by selling the issue on the same day he purchased it (i.e. the stock's effective date) or the day after, since the securities immediately sold at a substantial premium. In another 4 cases Pitt realized substantial profits by selling the issues 6, 8, 8, and 14, days, respectively, after purchase.[33/]

By definition and by their nature hot new issues are in the nature of a "sure thing" for the individual interested in a quick in-and-out profit. As soon as the stock has risen to a premium it is sold for a substantial profit. As already noted, Pitt in a number of cases sold the stock on the same day on which he purchased it, or the next day, whereas he didn't have to pay for the stock until it was delivered to Seattle Trust by the selling broker-dealer. While in other cases Pitt chose to hold some issues longer, presumably in the hope of maximizing his profits, the fact is that with respect to each hot issue he was in

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32/ The 10 hot issues purchased from Black Company and the one hot issue purchased from Pressprich are treated below in greater detail in the sections of this decision that consider the alleged violations of those two respondents and Black.

33/ All, or some, of the remainder of the 23 new issues purchased by Pitt may also have been "hot" issues, as an examination of the National Quotation Bureau Inc.'s "pink sheets" might disclose. Such an examination has not been made, however, for new issues other than those purchased from Black Company and Pressprich. See footnote 47 below.

a position to realize an immediate and substantial profit without having advanced any capital of his own.

In personally accepting allocations of hot new issues of stock from broker-dealers with whom he was conducting official business on behalf of SFC and the State Funds administered by SFC, it is abundantly clear that Pitt utilized his official position as Executive Secretary of the SFC to obtain special privileges for himself and that in so doing he also accepted, directly or indirectly, "compensation" or a "gift, reward, or gratuity" from sources other than the State of Washington within the meaning of the statutory prohibitions of the State of Washington set forth above. Further, acceptance of such allocations of hot issues involved Pitt in transactions and professional activity which placed him in conflict with the proper discharge of his duties in the public interest within the meaning of Section 42.22.030 of the Revised Code of Washington by placing Pitt into a conflict-of-interests position.

The Washington-State statutes flatly prohibit an official's acceptance of compensation, gifts, rewards, or gratuities, his obtaining of special privileges, or his placing himself into a conflict-of-interests situation in connection with his official duties. The statutes do not go further to require a showing that Pitt accepted such privileges, gifts, rewards, gratuities, or compensation as a quid pro quo for directing business to the respective broker-dealers.[34/]

34/ Cf. United States v. Deutsch, 451 F. 2d 98, (C.A. 2d 1971) at pp. 112, 113, cert. den. Jan. 10, 1972; Cf. Imperial Financial Services, Inc., 42 SEC 717, 727-8 (1965).

In addition to being subject to the above-quoted statutory prohibitions of the State of Washington upon receipt, directly or indirectly, of any compensation, gift, reward, or gratuity other than that provided by the State, and to the strictures that he not use his official position to obtain any special privileges for himself or his family and that he not engage in any transaction or activity on his own behalf that would conflict with the proper discharge of his public duties, Pitt, as an agent of the SFC, his principal, which had invested Pitt with broad discretion and authority in dealing on behalf of SFC, owed a fiduciary duty to the SFC and the State Funds managed by the SFC that Pitt violated.[35/] Thus, among Pitt's obligations as a fiduciary he had a duty to account to his principal, the SFC, for any profits (including gratuities) inuring to him out of his employment,[36/] the duty not to act adversely to the interests of the SFC without its consent,[37/] and the duty to deal fairly with the SFC in all transactions between them and to disclose to the SFC all relevant and material facts fully and completely.[38/]

35/ Restatement of the Law, Agency 2d, § 13.

36/ Id., § § 13,387,388. Comment b. under § 388 treats of gratuities to agents and states they may be retained by the agent if an agreement is found in custom or otherwise. With the possible exception of the Miami-Trip expenses, no agreement can be found here, for the SFC was completely unaware of Pitt's acceptance of other gratuities.

37/ Id., § § 13,389,390.

38/ Id., § § 13,381,390. Comment d. under § 381 (Duty to Give Information) states that if an agent has interests adverse to the principal as to matters within the scope of the agency he must reveal such facts to the principal. Comment a. under § 390 (acting as Adverse Party with Principal's Consent) states that in such situations the agent must ". . . disclose to the principal all relevant facts fully and completely. A fact is relevant if it is one which the agent should realize would be likely to affect the judgment of the principal in giving his consent to the agent . . . ."

The acceptance by Pitt of the allocations of hot new issues and his acceptance of unrepaid "loans" etc. was never disclosed by Pitt to the SFC, and the SFC was not otherwise aware of his receipt of these gratuities, until the entire practice was exposed and came under scrutiny and criticism in 1969 prior to Pitt's resignation under fire. One member of the SFC, the State Treasurer, was aware that Pitt had purchased some Rocket Research shares (not a new issue) during the relevant period, and may have been dimly aware that Pitt may have had other stock transactions for his own account, but none of the members of SFC was aware that hot new issues were involved in the practice or that Pitt was purchasing the stock through the Seattle Trust or utilizing his wife's checking account for the purpose. Nor was any member aware of the number of issues involved, Pitt's holding period, or the profits that he realized from the transactions. The receipt of unrepaid loans etc., likewise, was unknown to the SFC. These were all facts that were material facts 39/ within the concept of securities-law disclosure requirements that the SFC was entitled to know in order to form a conclusion whether the practice was flatly proscribed by law (as concluded above) and should be totally forbidden or whether the practice might be allowed in whole or in part under appropriate regulatory or supervisory safeguards.

Pitt does not contend that he advised the SFC of these practices or that the Committee members had knowledge of them from other sources.

39/ See cases cited in footnote 51 below.

It is concluded that Pitt's acts, practice, and course of business in accepting allocations of hot new issues of stock and of unrepaid "loans" etc., and his failure as a fiduciary to inform the SFC of such matters, in contravention both of the Revised Code of Washington and of his fiduciary duties as agent to his principal, the SFC, constituted, as charged, wilful[40/] violations by Pitt of the antifraud provisions of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, such violations having occurred in connection with the purchase and sale of various securities by use of jurisdictional means, i.e. the United States mails and interstate telephones.

Violations by Black Company and Black

During the relevant period Black Company sold to Pitt for his own account 10 new issues of stock, as shown on the schedule appearing on the following page. Each issue was sold at a profit, and the total profit on the sale of the 10 issues was $4,670.07. Of the 10 issues, 5 were sold within 4 days or less of purchase and another 2 were sold within 2 weeks of their purchase. While the record indicates that Black Company and Black were unaware how long Pitt may have held a particular stock before he resold it, the record does indicate that Black (and through him, Black Company) was well aware that Pitt's financial condition was such that he was unable to hold a large portfolio

40/ All that is required to support a finding of willfulness is proof that a respondent acted intentionally in the sense that he was aware of what he was doing and either consciously, or in careless disregard of his obligations, knowingly engaged in the activities which are found to be illegal. Hanley v. Securities and Exchange Commission, 415 F. 2d 589, 595-6 (2d Cir. 1969); NEES v. Securities and Exchange Commission 414 F. 2d 211, 221 (9th Cir. 1969); Dlugash v. Securities and Exchange Commission, 373 F. 2d 107, 109-10 (2d Cir. 1967); Tager v. Securities and Exchange Commission, 344 F. 2d 5, 8 (2d Cir. 1965).

SCHEDULE OF PITT'S PURCHASES AND SALES OF SECURITIES FOR HIS OWN ACCOUNT
FROM RESPONDENT BLACK COMPANY THROUGH SEATTLE TRUST

No. of Shares Purchased	Security (all new issues)	Trade Date (buy side)	Trade Date (sell side)	Holding Period	Purchase Price Per Share	Sale Price Per Share	Profit
50	Keuffel & Esser	9/14/65	9/28/65	14 days	$ 26.00	$ 26 7/8	$22.79
50	Barnes Hind	9/28/65	9/28/65	Sold same day	18.25	22.75	220.68
100	Data Processing	12/8/65	12/9/65	1 day	11.00	15.25	399.15
100	Western Microwave	12/7/65	12/11/65	4 days	22.00	31 1/8	912.50
100	Dearborn Computer	12/19/67	1/9/68	21 days	15.50	21.75	591.25
100	Yultide Enterprises	2/15/68	4/2/68 */	46 days	7.00	9.00	181.50
200	H.F. Image Systems	2/21/68	2/23/68	2 days	15.00	17.00	344.50
25	Integrated Containers	5/16/68	3/3/69	290 days	20.00	52.00	780.75
50	Ogden Corp. Conv. debs.	6/4/68	6/5/68	1 day	100.00	108.50	413.20
500	Zirconium Technology	2/12/69	2/25/69	13 days	5.50	7.25	803.75
						Total:	$4,670.07

*/ Although Exhibit 48 indicates that Pitt sold Yuletide Enterprises on 4/3/69 the date is obviously in error since Pitt's confirmation of this sale through L.F. Rothschild & Co. indicates that the sale took place on 4/2/68 (Ex. 56). See also Pitt's 1968 Tax Return (Ex. 38).

of stock for an appreciable length of time, and that therefore it was Pitt's general practice to hold the new issues only for relatively short periods of time. Put in other terms, Black was well aware that Pitt was not purchasing the stocks for long-term investment.[41/]

As noted earlier, Black Company received from Pitt during the relevant period on behalf of SFC securities business in an amount exceeding $1,600,000. More specifically, such purchases and sales transactions between Black Company and SFC occurred in the following amounts in the following months:

Mo./Yr. of Transaction	Total Purchases and Sales
11/65	203,474.99
2/68	478,572.90
3/68	493,003.45
4/69	471,418.75
	$1,646,470.09

In the context of the allegations of the Order, it is concluded that these allocations amounted to "substantial business."[42/]

As already noted above, all of the business Pitt did with Black Company, whether for the account of SFC or for Pitt's personal account, was handled through Black, the firm's president, executive officer, and principal owner. Black and Pitt had had business dealings on behalf of SFC from shortly after the time Pitt was appointed Executive Secretary of SFC in 1960, and in time the business relationship ripened into a combined business and social relationship.[43/]

41/ Although at least one stock was held for 290 days, it appears from the record as a whole that this was done by Pitt to maximize his profit and not because he was holding for the long-term as a general proposition.

42/ Although Black considered the SFC account small, he testified that he hoped and expected it to get substantially bigger.

43/ Mr. and Mrs. Pitt and their childeren visited the Blacks at their home in Lake Oswego, Oregon, a few times and Black and Pitt lunched and dined together occasionally.

Thus Black was fully aware of, and indeed he and Black Company were an integral part of, the practice under which Pitt purchased new issues of stock from Black Company through an account at Seattle Trust that did not disclose Pitt as the beneficial owner.[44/] Although Black knew Pitt was the true owner of the account, any books and records of Black Company that the Black Respondents were able to produce, e.g. confirmations of purchases sent to Seattle Trust, showed the account as that of Seattle Trust with no indication that Pitt was the beneficial owner.[45/]

Section 17(a) of the Exchange Act and Rule 17a-3 thereunder require every member of a national securities exchange and every broker-dealer registered under Section 15 of the Exchange Act to make and keep current, among other things, records that disclose the name of the customer for which each transaction is effected. In view of Black's personal knowledge of Pitt's true ownership of the account, Black Company's failure to reflect such ownership on its books and records was a wilful violation of the mentioned section and rule.[46/]

44/ Other, internal records of the Bank of course reflected Pitt's ownership of the account and the transactions that occurred therein on his behalf, but the Bank's broker-dealer account with Black Company did not reflect Pitt's ownership.

45/ The Black Respondents suggest that it may have lost "internal" records showing Pitt's beneficial ownership in the Seattle Trust account in the course of moving the firm's records from Oregon to New York and back; but this is speculation, since there is no satisfactory proof that Black Company ever made or kept a new account card, customer's ledger, or other record in Pitt's name.

46/ See footnote 40 for cases defining the criteria upon which a finding of wilfulness may be made under the federal securities laws.

The ten new issues sold by Black Company to Pitt during the relevant period, some of which were suggested to Pitt by Black, were all "hot" issues. As already noted above, a "hot issue" is generally recognized as an issue of securities that immediately or rapidly rises to a premium after the shares become available for trading in the secondary market.

Examination of Exhibit ALJ #14, 47/ which for 8 of the 10 issues shows the pink-sheet activity of the stocks for the ten business days following the date on which the new issues became effective, and which dates coincide with the dates on which Pitt purchased the securities, discloses that in each case the stock immediately or rapidly rose to a substantial premium.

Thus, Keuffel & Esser Co., purchased on 9-14-65 at $26.00 a share, was quoted on the bid side on 9-15-65 by one broker-dealer at 29 and by several at 28 7/8 or 28 3/4. On the 16th numerous broker-dealers showed bid quotes in the range of 28 7/8 to 28 1/4. Thereafter the stock continued to drop slightly each day until 9-28-65, when Pitt sold his shares at 26 7/8 per share. Had Pitt sold immediately, as he did in some instances, his gain would have been about 10% (without considering commissions).

47/ By order dated May 3, 1974, the Administrative Law Judge gave the parties notice of his intention, in accordance with 17 CFR 201.14(d), of the Commission's Rules of Practice, to take official notice of certain matters appearing in the Commission's public files or in the National Quotation Bureau's "pink sheets", copies of which were attached, designated for convenient reference as "Exhibit ALJ #10". Opportunity was afforded the parties to "establish to the contrary" by May 24, 1974. No party has filed a response. The reference to "Exhibit ALJ #10" was later corrected to "Exhibit ALJ #14" by order of June 24, 1974, since ALJ Exhibits 10 through 13 had already previously been received by prior orders. The use of the pink sheets to establish market price, in the absence of contrary evidence, was sanctioned in Charles Hughes & Co. v. SEC, 139 F. 2d 434, 438 (C.A. 2d 1943), cert. den. 321 U.S. 786. See also Rentz & Co. Inc. et al., 43 SEC 436, 437 (1967).

Barnes Hind, which Pitt purchased on 9-28-65 at $18.25 and sold the same day at $22.75, realizing an appreciation of some 24%, was quoted in the pink sheets on the bid side on 9-29-65 by 10 broker-dealers at from 23 1/4 to 23 3/4. Thereafter the stock showed moderate fluctuations until 10-12-65, when 16 broker-dealers quoted it on the bid side at from 24 1/4 to 24 5/8.

Data Processing, which Pitt bought on 12-8-65 at $11.00 and sold the next day at $15.25, at an appreciation of over 33%, showed a similar rise to a substantial premium immediately after it began trading in the secondary market. After jumping immediately from 11 to about 15 it continued to climb during the first 10 trading days until on 12-21-65 it was being quoted on the bid side at from 21 1/4 to 20 3/4.

Examination of Exhibit ALJ No. 14 further indicates that the following stocks Black sold to Pitt rose to an immediate premium after trading commenced in the secondary OTC market (with increases expressed in terms of approximate percentage of increase over the offering prices) as follows: Western Microwave, over 50%; Dearborn Computer, over 50%; Yultide Enterprises, over 35%; H.F. Image Systems, about 20%; and Integrated Containers, about 100%. On Ogden Corp. Conv. Debentures, which Pitt sold the day after purchase, the stock had risen to an 8 1/2% premium. Zirconium Technology, which Pitt sold 13 days after purchase, was selling at that time at a premium of about 30 per cent over its offering price.

The Black Respondents urge that the Division, which relied primarily on Pitt's purchase and selling prices, and the short holding periods in between, failed to establish that the 10 new issues allocated by Black

to Pitt were "hot" issues. In light of the supporting evidence reflected in Exhibit ALJ No. 14, there is no doubt but that all of the 10 new issues sold by Black to Pitt were hot issues.[48/]

The significance of the fact that the new issues sold by the Black Respondents to Pitt were hot issues, of course, lies in the circumstance that, as indicated previously above, it was possible to predict with reasonable certainty in advance whether a new-issue offering would immediately rise to a premium once the registration became effective and the stock began to sell publicly, depending upon the manifestations of interest that were being received by the underwriters before the effective date of the issue. Thus, once it becomes apparent that an issue will become a hot issue, an allocation thereof to an individual such as Pitt tends to be something of a "sure thing" or "money in the bank". This last characterization, given the way Pitt was operating through a bank account, was literally true.

Thus, the allegations in the Order that the Black Respondents allocated new issues to Pitt "with the expectation that the price would rise to a premium subsequent to the effective date of the offerings" is established by the record. As participating underwriters, the Black Respondents knew or should have known what the indications of interest in the stocks were before their registrations became effective. The actual results strongly tend to confirm that Black was allocating to Pitt new issues that he had every reason to expect would become "hot" issues.

48/ Only with respect to Zirconium Technology could it possibly be argued that the record fails to contain complete proof. However, the likelihood that such stock did not sell at a substantial premium directly after its registration became effective is remote in view of the fact that 13 days later it sold at an increase of about 30% and in light of the price patterns followed by the other 9 stocks.

Thus, the record establishes, as charged in the Order, that the Black Respondents "conveyed substantial benefits to Pitt" in connection with their receipt of substantial SFC business.

By allocating new issues that were expected to and did in fact became hot issues to Pitt personally, at a time when the Black Respondents were doing substantial state-fund business with the SFC through Pitt, the Black Respondents wilfully violated, and wilfully aided and abetted Pitt's violations of, the antifraud provisions of the Securities Act and the Exchange Act. The Black Respondents' participation[49/] in the fraudulent and deceptive acts, practice, and couse of business was an integral, indeed indispensable, element in such violations.

The Division also urges, as the Order alleges, that the Black Respondents violated the antifraud provisions of the Securities Act and the Exchange Act and aided and abetted their violation by Pitt through failing to disclose to the SFC that they were making allocations of hot new issues of stock to Pitt during the relevant period. The Division urges, in substance, that information as to such allocations was material, relevant information that should have been disclosed to the SFC so that the committee could have determined for itself whether it was proper or seemly for Pitt to continue to accept such allocations in light of his responsibilities under the Washington-State statutes and under the general law of agency, and, further, that if they had possessed such knowledge they would have been in better position to judge whether acceptance of such allocations by Pitt was improperly exerting any influence on his securities-buying procedures on behalf of SFC.

49/ And that of other respondents like the Black Respondents.

Assuming, as found above, that under the law and facts as found above Pitt's acceptance of allocations was flatly prohibited and clearly wilfully violated the antifraud provisions of the Securities Act and the Exchange Act, and that under the law and facts as found above the Black Respondents' participation in Pitt's acts, practices, or course of business clearly amounted to a wilful participation in and aiding and abetting of Pitt's violations of the antifraud provisions the fact of failure to have informed[50/] the SFC of the allocations to Pitt becomes in a sense academic.

However, assuming, arguendo, that the allocation to Pitt and his purchase of new issues expected to become hot was not per se a violation of the antifraud provisions, but that it did (as found herein) set up a situation that placed Pitt into an actual or potential conflict-of-interests position in light of his fiduciary obligations as an agent of the SFC, the failure by the Black Respondents to disclose their allocations to Pitt to the SFC does become significant and does constitute in itself a breach of the antifraud provisions.[51/]

50/ The Black Respondents concede they did not advise the SFC but urge they had a right to assume that Pitt did. In light of Black's close relationship to Pitt, Black's knowldge that the purchases for Pitt were being made through a Seattle Trust Account rather than in Pitt's name, and in light of the prohibitions of Washington State law, which Black knew of or should have known of, it is concluded that the Black Respondents had no reasonable basis for assuming that Pitt was keeping the SFC informed. For all their close contacts, the record shows that Black never even asked Pitt whether he had told SFC about his purchases of new issues.

51/ In this context the fact of the allocation of hot new issues to Pitt would clearly be a "material"fact. Cf. Affiliated Ute Citizens v. U.S. 406 U.S. 128, 154 (1972); Mills v. Electric Auto-Lite Co., 396 U.S. 375, 385 (1970). Accord, Chasins v. Smith Barney & Co., 438 F. 2d 1167, 1171 (C.A. 2, 1971); Gilbert v. Nixon, 429 F. 2d 348, 356 (C.A. 10, 1970); Securities and Exchange Commission v. Great American Industries, Inc., 407 F. 2d 453, 459-60 (C.A. 2, 1968)(en banc), certiorari denied, 395 U.S. 920 (1969); Securities and Exchange Commission v. Texas Gulf Sulphur Co., 401 F.2d 833, 849 (C.A. 2d, en banc, 1968).

In arguing against any obligation on their part to have disclosed to the SFC their allocation of new issues to Pitt, the Black Respondents make a number of contentions, the more salient of which are considered here.

The Black Respondents contend, among other arguments, that the new-issue allocations created no conflict-of-interests situation because the new issues purchased by Pitt were securities that he was legally prohibited from purchasing on behalf of the SFC funds and that there was therefore no "competition" between Pitt and the SFC for the particular securities. This argument misses the essential thrust of the Division's argument concerning the allocation and purchase of new issues, i.e. that, under the circumstances presented by the record the allocation of a new issue expected to become hot was as offensive as an outright cash gift would have been, or, as in the case of another of the settled-out respondents, a "loan" that wasn't expected to be repaid.

The Black Respondents further urge that the allocation of new issues to Pitt involved no giving of a gift: Pitt bought and paid for the stocks, ran the risk of loss on them, and his arrangements with the Seattle Trust were legal and proper. This argument overlooks the fact that, as found above, the risk of loss on these new issues was minimal. Because the risk was so minimal, the allocations were simply a highly sophisticated means of doing Pitt a favor or giving him a "gift" or "gratuity" in recognition of his ability as Executive Secretary of the SFC to direct SFC fund transactions to Black Company. The record does not permit a conclusion that Pitt would have been given these allocations of new issues even though he had not been Executive Secretary of the SFC, nor does the record establish that giving him such allocations was consistent

with the NASD's free-riding interpretation.[52/] While Black testified that after Pitt was Executive Secretary he expressed to Black an "interest" in new issues, and while Pitt testified that before becoming Executive Secretary of SFC and while he was associated with a broker dealer, he (or his wife) purchased perhaps a half dozen new issues from broker-dealers other than the one he was then working for, the record herein contains no indication that Pitt (or his wife) ever had an account with Black Company prior to the new issue purchases here involved or that he had established with Black Company a record of securities purchases such as would have entitled him to small new-issue allocations under the NASD free-riding interpretation notwithstanding his falling into a "restricted account" category because of his position as Executive Secretary of SFC. In any event, even if Black's allocations of hot new issues to Pitt had met the NASD's free-riding interpretation, this would not eliminate the obligations under Washington State statutes or the fiduciary obligations of an agent to his principal.

The Black Respondents also argue that if the Commission desires to impose reporting requirements on broker-dealers under circumstances similar

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52/ Section 1 of Article III of the NASD's Rules of Fair Practice requires the observance of high standards of commercial honor and just and equitable principles of trade. The NASD's Interpretation, as in effect in 1968, recited that members had an obligation to make a bona fide public offering, at the public offering price, of securities acquired by a participation in any distribution. Accordingly, if a member had unfilled orders from the public or had failed to make a bona fide public offering, it was a violation of Section 1 of Article III to sell any of its participation in new issues to specified restricted accounts unless the member could demonstrate that the allocations were in accord with the normal investment practices (other than in "hot" issues) of the accounts involved, and that the aggregate of the securities so allocated was insubstantial and not disproportionate in amount as compared to the member's sales to the general public.

For a discussion of the purposes underlying the NASD's free-riding interpretation see Rentz & Company, Inc. et al., 43 SEC 436, at pp 437-8, which characterizes the considerations underlying category (4) of the interpretation (the category here relevant by analogy) as being similar to those that underlie the NASD's "commercial bribery" rule.

to those disclosed by the record in this proceeding they should do so by exercising their rulemaking function rather than by adjudication. There is little, if any, merit to this argument. The Courts have long recognized that in circumstances such as these the Commission is free to proceed either by rulemaking or by adjudication.[53/] Secondly, at least three warning signs, i.e. the statutory Codes of Ethics of the State of Washington, the general fiduciary obligations of an agent such as Pitt to his prinicpal, and the NASD's free-riding interpretation, should have placed the Black Respondents on notice that they should have reported to the SFC their new-issue allocations to Pitt, under the circumstances here present, if they decided to make such allocations at all in face of the contraindications to doing so.

Accordingly, it is concluded that Black Company, having made allocations of new issues to Pitt under the circumstances found above, was under a legal duty to disclose such allocations to the SFC and that its failure to do so constituted a wilfull violation of the antifraud provisions of the Securities Act and the Exchange Act. Black aided and abetted such violations.

The Division also contends, as the Order alleges, that Black Company during the relevant period failed reasonably to supervise Black with a view to preventing the violations of the Securities laws committed by Black.[54/] This supervision, the Division contends, should have been

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53/ E.g. SEC v. Chenery, Corp., 332 U.S. 194, 202-3 (1947). See discussion of this issue as part of a more broadly-stated contention of various respondents, treated below at pp. 47 through 51 .

54/ Section 15(b)(5)(E) of the Exchange Act, as added by the 1964 amendments to it, provides an independent ground 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, [various securities statutes, including the Securities Act and the Exchange Act], rules, and regulations, another person who commits such a violation, if such other person is subject to his supervision."

carried out by the Board of Directors of Black Company.

There is no direct evidence in the record on the question of what supervisory powers, if any, the Board of Directors reserved to itself or exercised over Black, the firm's president, chief executive officer and principal owner, who was himself charged with overall supervision of the firm's employees. There would seem to be no reason in law or regulation why the firm's board of directors, as such, should as a matter of law be required to supervise Black in a matter such as is here involved, i.e. the allocation of new issues. So far as the record shows, overall supervision was assigned to Black and exercised by him.

Moreover, Black Company is vicariously subject to the imposition of sanctions predicated upon violations by Black both under § 15(b)(5) of the Exchange Act, since Black is a "person associated" with Black Company, and under the concept of Respondeat Superior.[55/] Indeed, the antifraud violations found above to have been committed by Black Company are based essentially upon the conduct of Black, a reflection of the fact that a corporate body can act only through its officers and employees and must therefore be responsible for their conduct within the scope of employment.

Under all of these circumstances it is concluded that it would be inappropriate to conclude that Black Company had failed reasonably to supervise Black within the meaning of Section 15(b)(5)(E) of the Exchange Act, and such charge is accordingly dismissed.[56/]

55/ Armstrong, Jones & Co. v. SEC, 421 F. 2d 359, 362 (C.A. 6, 1970), cert. den. June 15, 1970.

56/ To hold the firm liable on these facts for a failure to supervise Black would be to impose a species of liability without fault, whereas Section 15(b)(5)(E) liability is predicated upon a wilful or at least negligent failure to carry out supervisory obligations.

Violations by Pressprich

During the relevant period Pitt caused the SFC to engage in securities purchase and sale transactions totalling over $17,740,000 with Pressprich, an amount that clearly constituted "substantial business" within the meaning of that term as used in Section II E of the Order.

During that same period Pressprich allocated two new issues to Pitt for his personal use, which Pitt purchased through the Seattle Trust account. Of the two new issues, the first, Technitrol, purchased in April of 1966, was "hot", and the second, Integrated Container, purchased in March, 1969, was not.

Turning first to the second new issue, i.e. Integrated Container, the Division concedes, as the evidence establishes, that it was not a "hot" issue, but suggests that the respondents may have expected or anticipated it would be hot, i.e. that its price would rapidly rise to a premium when it began to sell publicly after the registration became effective. However, the record contains no satisfactory proof that either Pitt or Pressprich personnel anticipated it would become hot or were aware of facts that would have warranted a reasonable person to expect that it would become hot. Accordingly, it is concluded that the sale in 1969 of Integrated Container shares to Pitt does not support the antifraud allegations.

Pressprich concedes, as the record establishes, that the 100 shares of Technitrol it sold to Pitt through the Seattle Trust account in April of 1966 were part of a "hot" new issue. The salesman who

arranged the allocation of Technitrol shares by Pressprich to Pitt was in Pressprich's Portland, Oregon, office, and was one who did business with Pitt on behalf of SFC. This salesman was aware that because Pitt was in the category of "restricted accounts" within the NASD's free-riding interpretation because of his position as Executive Secretary to SFC, he could not allocate new-issue shares to Pitt (since Pitt at that time had no record of an established securities account relationship with Pressprich) without violation of then-existing policies of Pressprich.[57] Nevertheless, out of "friendship" for Pitt and because of Pitt's status as SFC's Executive Secretary, this salesman agreed to make the allocation of Technitrol shares to Pitt through his Seattle Trust account without disclosing to anyone in the Pressprich firm that Pitt was the beneficial owner of the Seattle Trust account. The Pressprich salesman was able to conceal the identity of Pitt as the true purchaser of the Technitrol shares from anyone at Pressprich because the manager of the Portland office of Pressprich at that time was a person who had had very limited experience in the securities industry[58] and was essentially a manager in

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57/ Pressprich's policy memorandum No. 26, issued in 1963 (Pressprich's Exhibit A) was in implementation of the NASD's free-riding interpretation, and forbade the allocation "directly or indirectly" of a hot issue to Pitt, a professional buyer of an investing institution, in the absence of an existing record of personal transaction with Pressprich other than in "hot" issues.

58/ His background was in banking.

name only, a fact that Pressprich's headquarters office in New York knew or should have known. Thus, allocations of new issues were made by salesmen in the Portland office without adequate review or supervision by the then manager. The salesman who sold the Technitrol to Pitt testified that he in fact did not look to the Portland manager but to the New York compliance office for supervision. Pressprich's compliance unit operated out of the New York headquarters office and at that time compliance efforts involved primarily about 4 inspection trips a year to the Portland office. These procedures were not reasonably adequate to have uncovered the salesman's deception respecting the sale to Pitt.[59/]

It is concluded that, particularly in view of the ineffectual managership in Pressprich's Portland office, and the failure to take into account Pitt's obligations to the SFC under state law and the common law, the then-existing system Pressprich had for establishing and applying compliance procedures could not reasonably be expected to prevent and detect, within the meaning of Section 15(b)(5)(E) of the Exchange Act, the wilful antifraud violations committed by its salesman in Portland and that, accordingly, appropriate sanctions may be applied to Pressprich for its failure reasonably to supervise if any sanctions are found indicated in the public interest.[60/]

59/ In matters of the kind here involved there is no adequate substitute for competent supervision by the branch manager. In addition Pressprich's supervisory policies and procedures at no point reflected or took into account the special Washington State statutory provisions relating to Pitt or to the fiduciary obligation Pitt owed the SFC as its agent.

60/ Pressprich's failure adequately to supervise a person under its control also caused it to wilfully violate Section 17(a) of the Exchange Act and Rule 17a-3 thereunder by failing to disclose in its books and records Pitt as the true purchaser of the Technitrol new issue in 1966.

The Division also points out, correctly, that under Section 15(b)(5)(D) of the Securities Act sanctions may be applied, if found to be in the public interest, against Pressprich on the basis of the wilful violations of the antifraud provisions of the Securities Act and the Exchange Act found to have been committed by its Portland salesman, a "person associated with" Pressprich within the meaning of the mentioned section. While this position is technically correct, it is concluded, under the circumstances applicable to the Pressprich violations, that it would be appropriate in the public interest to impose any sanction that may be warranted on the basis of Pressprich's failure to supervise, since that is the true gravamen of the charges against it, rather than on the basis of sanctions predicated upon a type of "derivative" liability without fault.[61/]

61/ In this connection it is of interest to note the Commission's action in a converse situation in Anthony J. Amato, et al., Exchange Act Release No. 10265, June 29, 1973, where the Commission declined to affirm an NASD finding of failure to supervise where the NASD had also found, and the evidence established, active violative participation. The Commission stated, at p. 5:

> "We shall, however, set aside the NASD's finding that Bills failed to exercise proper supervision. That finding is inconsistent with the active role Bills himself played in his office's involvement and in that of his subordinates in the Bubble Up transactions. Failure of supervision -- which may result in derivative responsibility for the misconduct of others -- connotes an inattention to supervisory responsibilities, a failure to learn of improprieties when diligent application of supervisory procedures would have uncovered them. That is not the situation here. In view of Bills' active and central role in the whole matter, affirmance of the finding of failure to supervise would entail a confusion of concepts."

See also In the Matter of the Application of Jerome F. Tegeler, Exchange Act Release No. 10747, April 19, 1974, p. 4, particularly footnotes 8-10 and text thereto.

The Division also urges that the wilful antifraud violations of Pressprich's Portland office registered representative in selling the Technitrol hot issue to Pitt are in law wilful violations of such provisions by Pressprich under the concept of respondeat superior, which holds in essence that wilful violations by an employee in the scope of his employment are the wilful violations of the employer.[62-64/]

Pressprich argues that the concept of respondeat superior should not be applicable in an enforcement proceeding (as distinguished from litigation between private persons) and that instead the "good faith" standard set forth in Section 20(a) of the Exchange Act should control,[65/] citing SEC v. Lum's, Inc., et al., 365 F. Supp. 1046, 1061-65 (U.S.D.C. S.D.N.Y., 1973).

While Lum's (a suit by the SEC to enjoin) supports Pressprich's position, an analysis of the case indicates it was wrongly decided. The cases relied on in the decision involve litigation between private

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62-64/ Armstrong Jones & Co. v. SEC, 421 F.2d 359, 362 (C.A. 6, 1970), cert. den. June 15, 1970; SEC v. Charles A. Morris & Associates, Inc. CCH Fed. Sec. L. Rep. Para. 93, 756 at pp. 93,305-93,306; Sutro Bros. & Co., 41 S.E.C. 470, 479 (1963); Cady Roberts & Co., 40 S.E.C. 907, 911 (1961); H.F. Schroeder & Co., 27 S.E.C. 833, 837 (1948).

65/ "LIABILITIES OF CONTROLLING PERSONS

"Sec. 20. (a) Every person who, directly or indirectly, controls any person liable under any provision of this title or of any rule or regulation thereunder shall also be liable jointly and severally with and to the same extent as such controlled person to any person to whom such controlled person is liable, unless the controlling person acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action." (emphasis added).

persons and not administrative enforcement proceedings or litigation involving the Government. The language of Section 20(a), which defines the liability of a controlling person in those cases in which the controlled person is liable "to any person" may suggest that the "good faith" defense applies to litigation involving liability of one "person" [66/] to another and not to enforcement proceedings by the Commission or other enforcement agency of the Government.

Further, this proceeding is brought under Section 15(b) and not under Section 20(a) of the Exchange Act, which was also the situation in the Lum's case, and the Lum's Court gives no satisfactory rationale for regarding the latter section as controlling when the proceeding is brought under the former, nor for disregarding the long-standing Court of Appeals decision in Armstrong, Jones, cited above, which expressly affirmed the continued applicability of respondeat superior to the Commission's administrative proceedings under Section 15(b) of the Exchange Act in the face of an argument that liability should be tested under the failure to supervise standards of §15(b)(5)(E),added in 1964.

Moreover, at least one Court has concluded that the "good faith" standard of Section 20(a), even in suits between private individuals, does not apply to the employer-employee relationship.[67/] This case, brought under Section 12(2) of the Securities Act, held partners of a

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66 / "Person" as defined in Section 3(a)(9) of the Exchange Act does not include the Commission or any other enforcement agency.

67 / Johns Hopkins University v. Hutton, 297 F. Supp. 1165, 1211-2 (D. Md. 1968), rev'd in part and aff'd in part, including the point here relevant, 442 F.2d 1124, 1130 (C.A. 4th, 1970).

broker-dealer liable to a third party for frauds of the firm's employees after concluding that the "good faith" standard of Section 20(a) of the Exchange Act did not apply to the employer-employee relationship.[68/]

Yet another weakness in the Lum's decision is that, while it discusses the question of failure to supervise in the context of discussing the need for finding at least negligent conduct as a prerequisite to the imposition of liability, it nowhere mentions or considers Section 15(b)(5)(E) of the Exchange Act, as added in 1964, which obviously sets forth the controlling provisions regarding imposition of administrative sanctions for a failure adequately to supervise. Instead, the Court, at p. 1065, determines the issue respecting lack of supervision in terms of the "good faith" defense of Section 20(a).[69/]

Accordingly, it is concluded that Section 20(a) does not restrict the concept of respondeat superior as applied in the Commission's

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68/ The Court stated at pp. 1211, 1212 its conclusion as follows: "What legislative history there is does not indicate that Congress intended Section 15, originally or as amended, to serve as a limitation on liability. [footnote omitted]. The section would seem, on the other hand, to have been intended to establish a 'controlling person' liability which would supplement, and extend beyond, common law principles of agency and respondeat superior." 297 F. Supp. at 1211-1212, aff'd. on this point, 422 F.2d at 1130.

Johns Hopkins has been cited for the proposition that the controlling-persons sections of the 1933 and 1934 Acts are not exclusive. It has led at least one commentator to remark that:

> "It seems likely that . . . the specific defenses of the controlling persons sections of the 1933 and 1934 Acts will be available only in those situations in which use of those sections is necessary to impose liability. If other theories of liability such as agency, aiding and abetting conspiracy, or direct participation are used, then the 'special' defenses of the controlling persons sections will apparently be unavailable." Ruder, "Multiple Defendants in Securities Law Fraud Cases: Aiding and Abetting, Conspiracy, In Pari Delicto, Indemnification, and Contribution," 120 U. Penn. L. Rev. 597, 608 (April 1972).

69/ For a critique of the Lum's decision see Note, The Burden of Control: (Continued)

administrative proceedings under the Armstrong, Jones and Charles A. Morris & Associates, Inc. decisions, above, and numerous Commission decisions.[70] Further, it is concluded that the wilful violations commited by Pressprich's Portland office registered representative were committed in the "course of employment" in that he acted for the firm, even though he violated the firm's internal policies in so doing.

While, therefore, it must be concluded that under the concept of respondeat superior Pressprich wilfully violated, and aided and abetted Pitt's violations of, the antifraud provisions of the Securities Act and the Exchange Act, it is concluded that, for reasons already stated above in connection with discussion of Pressprich's liability to the imposition of sanctions because of the violations of its "associated person" (see p. 38 above), under the circumstances applicable to the Pressprich violations, it would be appropriate in the public interest to impose any sanction that may be warranted on the basis of Pressprich's failure to supervise rather than under the respondeat superior doctrine.

69/ (Continued)
Derivative Liability under Section 20(a) of the Securities Exchange Act of 1934, 48 New York University Law Review 1019 at pp. 1032 - 1034 (November, 1973).

70/ For a view that questions in part the basis for and continuing strength of Armstrong, Jones, see Note, 48 New York University Law Review, cited in footnote 69 above, particularly portions dealing with "Secondary Liability Under Common Law" at pp. 1029-1031, "A Suggested Approach: The Variable Good-Faith Standard" at pp. 1034-1039, and "Conclusion" at pp. 1041-1042.

Contentions of the Respondents

In addition to the contentions of Respondents considered above, some or all of the Respondents make additional contentions that call for treatment herein.

1. Statutes of Limitation

Respondents contend that any charges predicated on events that occurred more than 5 years prior to the Order for Proceeding are barred by the statute of limitations on civil penalties or forfeitures contained in 28 U.S.C. §2462, [71/] relying upon the decision in H.P. Lambert Co. v. Secretary of the Treasury, 354 F.2d 819, 822 (C.A. 1st 1965).

Lambert involved a revocation of a customhouse broker's license by the Secretary of the Treasury under 19 U.S.C. §1641(b) on the basis of alleged misconduct that occurred, at least in part, more than five years prior to initiation of the revocation proceeding. Rejecting the Treasury Department's argument that §2462 was not applicable because 19 U.S.C. §1641 "otherwise provided", the Court held §2462 applicable without discussing the broader question whether a statute of limitations set forth in title 28 U.S.C., concerning the Federal Judiciary and

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71/ Section 2462 reads as follows:

"§2462. Time for commencing proceedings

Except as otherwise provided by Act of Congress, an action, suit or proceeding for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise, shall not be entertained unless commenced within five years from the date when the claim first accrued if, within the same period, the offender or the property is found within the United States in order that proper service may be made thereon. June 25, 1948, c. 646, 62 Stat. 974."

Historical and Revision Notes

Reviser's Note. Based on Title 28 U.S.C., 1940 ed., §791 (R.S. §1047). Changes were made in phraseology. 80th Congress House Report No. 308.

Judicial Procedure applies to administrative proceedings under the Administrative Procedure Act, saying ". . . the general policy of statutes of limitations is so deeply ingrained in our legal system that a period of limitations made generally applicable to such proceedings, as is Section 2462 is not to be avoided unless that purpose is made manifestly clear."

The Commission has held the statute of limitations set forth in 28 U.S.C. §2462 inapplicable to its administrative enforcement proceedings under the Exchange Act in an unpublished "Memorandum Opinion and Order" dated August 11, 1952,[72/] issued in In the Matter of Thomson & McKinnon and Jack Karn, 35 S.E.C. 451. The bases for the conclusion in the Commission's Memorandum Opinion, which a recognized writer in the field of Securities Law considers "sound",[73/] include, among other points: the observation that the Judicial Code, 28 U.S.C., which was revised and enacted into positive law in 1948, deals with Federal Courts and their jurisdiction and procedure, and there is nothing therein or in its legislative history to suggest that its provisions would govern administrative enforcement proceedings under the Exchange Act, which, instead, are governed by that Act and the Administrative Procedure Act of 1946; the

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72/ The memorandum opinion is attached hereto as Appendix B. Since the proceeding was private, the record therein did not become public until the Commission's decision in the proceeding was issued.

73/ Loss, Securities Regulation, 2d ed., Vol. II, p. 1174, footnote 10.

fact that while the Exchange Act prescribes limitation periods with respect to certain civil actions thereunder, it contains no provision limiting the bringing of Commission enforcement actions, and the APA, enacted as a pervasive, comprehensive code of procedure for administrative agencies, contains no limitation period, even though that would have been the logical place for the Congress to express any general limitation period for administrative enforcement proceedings that it might have desired; and the point that the Commission's enforcement proceedings, in which the imposition of sanctions is conditioned expressly on a finding that their imposition would be in the public interest, are remedial in character and therefore not penalties within the meaning of 28 U.S.C. §2462.

On the basis of the Commission's conclusion in its Memorandum Opinion in Thomson & McKinnon, above, and on the basis of independent examination of the principles of legislative construction, it is concluded that the Lambert case is not persuasive, and that 28 U.S.C. §2462 does not limit administrative enforcement proceedings of the Commission under the Exchange Act or the Securities Act.

Even if 28 U.S.C. §2462 otherwise were applicable to the Commission's enforcement proceedings under the Exchange Act, the section would be inapplicable because the Exchange Act "otherwise provides" within the meaning of §2462. Thus, Section 15(b)(5) of the Exchange Act permits the imposition of sanctions against a broker-dealer based on derelictions committed by a person associated with such broker-dealer, whether prior or subsequent to being so associated, without any time limit on the prior misconduct. Similarly, in §15(b)(5)(B), Congress evidenced that it knew how to spell out a time limit on misconduct when it chose to do so, by

setting a 10-year limit on the use of described felony or misdemeanor convictions as a basis for sanctions in certain specified cases. Moreover, as noted by the Commission's Memorandum Opinion in Thomson & McKinnon, above, the fact that Congress spelled out limitation periods in civil suits between private parties under the Exchange Act but set no overall limitations period for enforcement proceedings by the Commission strongly indicates that Congress intended no such limitations period to be applicable to enforcement proceedings.

The Black Respondents also contend that the three-years-from-discovery limitations statute for fraud of the State of Washington (Revised Code of Washington, 4.16.060) applies to this proceeding. They cite no authority for applying that statute in a federal enforcement proceeding as distinct from its use in private civil actions for damages under Rule 10b-5. The Commission has held that state statutes of limitation do not apply to its proceeding under §15(b) of the Exchange Act.[74/] It is concluded that this defense is without merit.

2. Contention That Commission is Attempting to Enforce Washington - State Laws and NASD Rules

Some of the respondents urge that by bringing this proceeding the Commission is improperly endeavoring to enforce the statutory law of the State of Washington and/or the NASD's free-riding interpretation. There is no merit to these contentions. The charges in the Order are all specific charges of violations of specified federal antifraud provisions,

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74/ Richard N. Cea, et al., Exchange Act Release No. 8662, August 6, 1969, at p. 12; see also Board of Commissioners v. U.S., 308 U.S. 343, 351 (1939).

record-keeping requirements, and the requirement reasonably to supervise. It is only violations of those provisions or requirements that are found herein. This is not to say that in determining whether a fraudulent or deceptive act, practice, or course of business has occurred within the meaning of federal laws and regulations the Commission may not look to duties or prohibitions placed upon a respondent by state statutes or by the common law applicable to a given legal status that a particular respondent may have had. Nor does it mean that the Commission may not look to the NASD's free-riding interpretation, and respondents' knowledge thereof, as an element in determining whether particular conduct on the part of a respondent as established by the record was wilful or in determining the extent of sanctions, if any, that should be imposed in the public interest.

What Respondents' argument overlooks, basically, is that a given act, practice, or course of business may be in contravention of both state and federal statutes and/or regulations, the common law, and regulations of a self-regulatory industry body. But this does not alter the fact that the only laws and regulations under which violations in this proceeding have been charged and found are federal securities laws and regulations.

3. Contention that Commission Seeks to Impose Sanctions Retroactively by Adjudication That Properly Should Only be Applied Prospectively Through Rulemaking

Some respondents, particularly the Black Respondents, contend that a finding of violations on their part in this proceeding would in effect constitute retroactive promulgation of a rule of conduct for broker-dealers that properly the Commission could only adopt prospectively through

rulemaking procedures. They ask, perhaps rhetorically, what rule of conduct for broker-dealers an attorney could derive from adverse findings in this proceeding for purposes of advising his broker-dealer clients as to their future conduct.

These arguments lack validity. The antifraud provisions and the record-keeping requirements found to have been violated long antedated in their promulgation the course of conduct here involved. What these Respondents are really arguing is that Rule 10b-5 sets forth standards in its definition of fraud that are too general and that the Commission should prescribe a specific rule forbidding or regulating the sale by broker-dealers of new issues or hot new issues to representatives of institutional investors for their personal accounts while doing business with such institutional investors through such representatives, if the Commission should desire to regulate such personal transactions with representatives of institutional investors.

This argument ignores the fact that the Courts have long held that the choice between proceeding by detailed rulemaking or by ad hoc adjudication is one that lies primarily in the informed discretion of the administrative agency. SEC v. Chenery Corp., 332 U.S. 194, 202-3 (1947). In Chenery, the Supreme Court stated in pertinent part, at pages 202 and 203, as follows:

> ". . . Not every principle essential to the effective administration of a statute can or should be cast immediately into the mold of a general rule. Some principles must await their own development, while others must be adjusted to meet particular, unforeseeable situations. In performing its important functions in these respects, therefore, an administrative agency must be equipped to act either by general rule or by individual order. To insist upon one form of action to the exclusion of the other is to exalt form over necessity."

" . . . . Or the problem may be so specialized and varying in nature as to be impossible of capture within the boundaries of a general rule. In those situations, the agency must retain power to deal with the problems on a case-to-case basis if the administrative process is to be effective. There is thus a very definite place for the case-by-case evolution of statutory standards. And the choice made between proceeding by general rule or by individual, ad hoc litigation is one that lies primarily in the informed discretion of the administrative agency. See Columbia Broadcasting System v. United States, 316 U.S. 407, 421."

What the Court said in Chenery is particularly applicable to the definition of securities fraud, which seems to take form in a seemingly infinite number of factual variants, mutations, and permutations.[75/]

In the instant proceeding the Black Respondents appear to concede that "cultivating" Pitt with outright gifts of money could be determined to be an antifraud violation, at least if the "in connection with" requirement, discussed later herein, is met. Under the circumstances

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75/ As the Commission stated in Cady, Roberts & Co., 40 S.E.C. 907, 911 (1961), the antifraud provisions of Section 17(a) of the Securities Act and Rule 10b-5 of the Exchange Act ". . . are not intended as a specification of particular acts or practices which constitute fraud, but rather are designed to encompass the infinite variety of devices by which undue advantage may be taken of investors and others." In a footnote to this statement, the Commission observed:

"12. It might be said of fraud that age cannot wither, nor custom stale its infinite variety."

In Investors Management Co., Inc., et al., Exchange Act Release No. 9267, July 29, 1971, the Commission stated, at pp. 14-5: ". . . . The ambit of the antifraud provisions is necessarily broad so as to embrace the infinite variety of deceptive conduct."

See S.E.C. v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 195 (1963). Cf. Chasins v. Smith Barney & Co., Inc., 438 F.2d 1167 (C.A. 2, March 2, 1971); Opper v. Hancock Securities, 200 F. Supp. 668, 676 (S.D.N.Y. 1966), aff'd 367 F.2d 157 (C.A. 2, 1966).

disclosed by this record the sale to Pitt of "hot" new issues, though far more subtle a means, was designed to achieve the same end of courting Pitt and was just as fraudulent and deceptive a practice as a cash gift would have been.[76/]

The record herein belies the Black Respondents' argument, express and implied, that they had no notice or reason to suppose that their sale of "hot" issues to Pitt might constitute a fraudulent or deceptive practice or course of business. Firstly, the plain language of the Washington State statutes cited and discussed above precluded Pitt's acceptance of such gifts or privileges.[77/] Moreover, common-law duties of the agent to his principle forbade Pitt's acceptance of "hot" issue gifts at least without disclosing them. In addition, the record contains no satisfactory proof that Pitt would have been entitled to purchase "hot" issues within the NASD's free-riding interpretation, since there is no proof of the required prior record of purchases in any Pitt account with Black Company.

At the very least, in light of all these existing contraindications to the sale of "hot" issues to Pitt, the Black Respondents should have fully informed the SFC that they were making or proposing to make "hot"

76/ Indeed, it can plausibly be concluded that the more subtle form of wooing is more pernicious than a more blatant or overt form on the ground that many representatives of institutional investors who would shrink from the latter might be beguiled by the former.

77/ None of the parties has presented any state case law construing the pertinent sections, nor have any cases been found in the annotations to the sections set forth in Appendix A.

The Washington State statutes discussed above are by no means unique. for a discussion of three federal statutes barring gratutities to federal officers or to affiliated persons of registered investment companies, see the Court's language in U.S. v. Deutsch, quoted at p.53 below. The principal underlying these statutes is as old as the biblical admonition that a man cannot serve two masters.

new issue sales to Pitt. Such information would have been highly relevant and material to the SFC for it would have enabled that committee, among other things, to make judgments whether such purchases were (a) legal, (b) desirable from the standpoint of public policy and of appearances to the public, and (c) were creating or would create an intolerable conflict-of-interests problem for Pitt or were exerting or would exert negative influences on Pitt's handling of official transactions for SFC.[78/]

In sum, the selling of "hot" new issues to Pitt was either participation in and in aid of a fraudulent practice in itself, as found above, or of such doubtful legal validity that the full circumstances surrounding it should have been disclosed to the SFC, in which case the failure to make such disclosure as required by the circumsances amounted to participation in and aiding and abetting a fraudulent or deceptive practice.[79/]

78/ In point of fact, subsequent to Pitt's resignation, the SFC adopted in November, 1970, a set of "Guidelines to Ethical Conduct" for its staff which, among other things, required staff officers and employees to disclose fully to the SFC any conflict of interests they might have; prohibited their ". . . purchase of new issues at the original public offering, other than mutual funds or U.S. government securities . . ."; and prohibited use of banks or other intermediaries as conduits for the purchase of securities. Exhibit 34.

79/ Various Respondents urge that they had a right to assume that Pitt was making disclosures to the SFC, but nothing in the record indicates that any respondent ever asked even Pitt, let alone the SFC, whether such disclosure was being made. In fact, as already found above, the SFC was unaware of Pitt's purchases of "hot" issues.

4. Contentions that Under the "In-Connection-With" Language of the Order There Must be Proof of Causal Relation Between Allocations of Hot Issues to Pitt and Quantum of Business Done by Broker-Dealers with SFC.

Certain respondents, particularly the Black Respondents, contend that under the allegation in Section II C of the Order that "in connection with" respondents' sales of "hot" new issues to Pitt they received "substantial business" from the SFC, the Division must prove a causal connection between the allocation of "hot" issues and the amount of SFC business received by Respondent Broker-Dealers. The Division denies this contention and urges that instead it is sufficient to show that Pitt received undisclosed (to the SFC) "compensation" or "gifts" in the form of "hot" new issues during a time when he was transacting substantial official business with Respondent Broker-Dealers on behalf of SFC, since Pitt's receipt of such "gifts" placed him in a conflict-of-interests situation that constituted part of a deceptive or fraudulent practice without any need to prove the mentioned causal connection. The Division stated its view on this point during the hearing and did not attempt to introduce any evidence establishing a causal connection.[80/] In support of its view on this point the Division cites U.S. v. Deutsch[81/] and Imperial Financial Services, Inc.[82/]

While the Deutsch case is a criminal case that arose under Section 17(e)(1) of the Investment Company Act of 1940, its holding and language are pertinent here by analogy in view of the comparability in their thrust and purpose of the respective statutes involved in that

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80/ The Division stipulated that it does not question any transaction between a broker-dealer respondent and the SFC with respect to quality, suitability, price, or timing of execution.

81/ 451 F. 2d 98 (C.A. 2d 1971), cert. den. 92 S. Ct. 682 (1972).

82/ 42 S.E.C. 717 (1965).

case and in this proceeding. The Court in Deutsch, at pp. 112-113, stated in pertinent part as follows:

> "The language of § 17(e)(1) makes no mention of intent to influence; the subsection is cast in the familiar 'for' terminology of the gratuity statutes (e. g., 18 U.S.C. §§ 201 (f-i) (1964)) where the only intent required is that the payment be given and accepted in appreciation of past, or in anticipation of future, conduct. We have held that intent to influence is not an element of 26 U.S.C. § 7214 (a)(2)(1964), which makes it a crime for a federal officer 'acting in connection with' the revenue laws to receive 'compensation . . . for the performance of any duty.' United States v. Cohen, 387 F. 2d 803, 806 (2 Cir. 1967), cert. denied, 390 U.S. 996 (1968). Similarly, we have held that the government does not have to show intent to influence to prove an offense under 18 U.S.C. § 201 (f)(1964), which makes it a crime to give a public official something of value 'for and because of any act performed or to be performed.' United States v. Irwin 354 F 2d 192, 197 (2 Cir. 1965), cert. denied, 383 U.S. 967 (1966). See also, United States v. Umans, 368 F.2d. 725, 730 (2 Cir. 1966), cert. dismissed as improvidently granted, 389 U.S. 80 (1967)."
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> "[10] The statute in the instant case is similar in this respect to the gratuity statutes. We do not believe that Congress intended that intent to influence should be read into § 17(e)(1) of the Act. The paying of compensation is an evil in itself, even though the payor does not corruptly intend to influence the affiliated person's acts, for it tends to bring about preferential treatment in favor of the payor which can easily injure the beneficiaries of investment companies. Congress recognized that affiliated persons had manifold opportunities for self-dealing and designed a statute to remove the potential for conflicts of interest by prohibiting the receipt of compensation 'for the purchase or sale of any property . . .' 15 U.S.C. § 80a-17(e) (1) (1964). We hold that to read into §17(e)(1) a requirement of intent to influence would frustrate this statutory purpose." (emphasis added).

In Imperial Financial Services, Inc., cited in note 82 above, the Commission concluded, at pp. 727-8, as follows in a proceeding also involving Section 17(e)(1) of the Investment Company Act of 1940:

> "Section 17(e)(1) of the Act is designed to prevent the receipt, by any affiliated person acting for the investment company, of any compensation in connection with the purchase or sale of investment company assets other than his regular salary or underwriter's or broker's fees. [footnote omitted]. As registrant's trader and a member of its Investment Committee, Foster was in a position to influence the choice of broker-dealers who would receive business from the transactions in Imperial's portfolio securities. We find that in accepting benefits, in the form of an interest-free loan and a discount price on the purchase of certain shares, from persons to whom commissions with respect to such transactions were directed, Foster received compensation in violation of Section 17(e)(1) of the Investment Company Act." [footnote omitted] (emphasis added).

It is concluded that the Order utilized the "in connection with" language in the sense that such or similar language is employed in the "gratuity" or similar statutes (see quote from Deutsch case, above, at p. 53 [83]), including, specifically the Washington State gratuity statutes,

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83/ In light of the factual situation involved in the charges contained in the Order, it is evident that the "in connection with" language under discussion was intended to convey the same loose connection as the same term does when used in the antifraud provisions of Section 10(b) of the Exchange Act to establish the necessary jurisdiction. This last "in connection with" clause "is plainly and-- one must assume-- intentionally the loosest linkage, in any of the federal antifraud provisions, between a proscribed act and a security transaction." Bromberg, Securities Law: Fraud-SEC Rule 10b-5, Sec. 7.6(1), p. 190.21 (1969). See, e.g., Herpich v. Wallace, 430 F. 2d 792 (C.A. 5); Kahan v. Rosenstiel, 424 F. 2d 161, 172 (C.A. 3), certiorari denied sub. nom. Glen Alden Corp. v. Kahan, 398 U.S. 950 Hooper v. Mountain States Securities Corp., 282 F. 2d 195 (C.A. 5), certiorari denied, 365 U.S. 814. Cf. S.E.C. v. Texas Gulf Sulfur Co., 401 F. 2d 833, 860 (C.A. 2d 1968).

and that proof of a fraudulent or deceptive act, practice, or course of business in this proceeding therefore does not require proof of a causal connection between the "hot" new issue "gifts" to Pitt and the amount of SFC business received by the allocating broker-dealer respondents. Nor does the charge require proof that Respondent broker-dealers had an intent to influence Pitt in his SFC decisions.[84/]

Accordingly, it is concluded that this contention of the Respondents is without merit.

Conclusions

In general summary of the foregoing, it is concluded that within the relevant period from about September 1965 to about October 1969: (1) Respondent Roy A. Pitt, Jr. wilfully violated the antifraud provisions of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder; (2) Respondents Black & Company Inc. and Lawrence S. Black wilfully participated in, and wilfully aided and abetted Pitt's violations of, such antifraud provisions, and wilfully violated the record-keeping requirements of Section 17(a) of the Exchange Act and Rule 17a-3 thereunder; and (3) Respondent R.W. Pressprich & Co. failed reasonably to supervise, within the meaning of Section 15(b)(5)(E) of the Exchange Act, a registered representative in its Portland office

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84/ The record does establish, as found above, that the hot new issues were allocated to Pitt because of his status as Executive Secretary of SFC, or, in the language of the Deutsch decision, quoted above at p. 53, that the allocations were made in appreciation of past, or in anticipation of future, awards of SFC business by Pitt. However, in light of the flat prohibitions of the Washington-State laws and the duties under common laws of Pitt as an agent, all that need really be shown is that the undisclosed gratuities to Pitt were made during a period when Pitt was awarding SFC business to Respondent broker-dealers.

subject to its supervision who during the relevant period wilfully participated in and wilfully aided and abetted Pitt's violations of the mentioned antifraud provisions.[85/]

PUBLIC INTEREST

The seriousness of the violations found in this proceeding is reflected in Sections 42.21.010 and 42.22.010 of Title 42 of the Revised Code of the State of Washington, which sets forth the "Declaration of necessity and purpose" of the Codes of Ethics for Public Officials and for Public Officers and Employees set forth in Chapters 21 and 22 of Title 42.[86/] When these purposes are coupled with the underlying purposes of the Federal securities laws to maintain public faith and confidence in the securities markets and, in particular, in systems and procedures involving institutional investors, the gravity of the violations is the more apparent.

Counterbalancing the gravity of the violations to some degree is the consideration that the factual circumstances involved in the violations are to a degree novel, even though the underlying legal concepts are not; the Commission has in the past taken the novelty factor into account in assessing sanctions.[87/]

85/ Pressprich also wilfully participated in and aided and abetted Pitt's antifraud violations under the respondeat superior doctrine and committed record-keeping violations, as found above, but, for reasons already indicated, the gravamen of Pressprich's misconduct for the purpose of assessing sanctions is considered to be its failure reasonably to supervise.

86/ See Appendix A, and pp.14-5 above.

87/ See Investors Management Co., Inc. et al., Exchange Act Release No. 9267, July 29, 1971, at pp. 14, 15, where the Commission affirmed the Administrative Law Judge's sanctions that had taken the novelty factor, among others, into account.

The violations committed by Pitt were numerous, extended over a considerable period of time, and ran the range from outright acceptance of cash ("loans" that were not repaid and were not expected to be repaid) to the more sophisticated receipt of virtually sure profits through acceptance of allocations of "hot" new issues. While the gifts and profits from the hot issues fell far short of making Pitt a wealthy man, the profits were not insubstantial and certainly not de minimus. Pitt was experienced in the securities business, and the inherent impropriety of his acceptance of various gifts, favors or gratuities should have been evident to him. The effects of his misconduct on the public confidence in the manner in which the SFC's public funds were administered is not calculable but must surely have been substantial, and negative, in view of the widespread and prolonged publicity that the matter received in the State of Washington. This is so even though there is no evidence in this record that the funds administered by the SFC and Pitt sustained any losses or were maladministered.

In Pitt's favor by way of mitigation of sanctions are the fact that he never before October 1970 has been the subject of any disciplinary proceeding for securities law violations brought by the Commission or any self-regulatory body and the fact that the publicity that attended his derelicitions caused him to become something of a pariah, with the result that he has been unable to obtain employment in the securities business or directly related endeavors except for one brief period of employment on a temporary basis with Black Company. Thus, in effect, he has had a de facto suspension for a considerable period.

In light of all the mitigative circumstances mentioned above and others urged by Pitt, it is concluded that as to him a bar with permission to apply for readmission to the securities business after a period of 9 months in a non-proprietary, non-supervisory capacity, subject to adequate supervision, would be an appropriate sanction in the public interest.

On the question of sanctions, the Black Respondents urge, among other things, that the sanctions proposed by the Division -- a suspension of Black for 90 days and a suspension of Black Company's registration for 30 days only insofar as its institutional type of business is concerned -- would cripple or annihilate the firm. In this connection the Black Respondents argue that Black Company is the only Oregon-headquartered firm in the Oregon area that is a member of the NYSE and that of all Oregon-headquartered broker-dealer firms it has the largest volume of corporate financings and underwritings. They urge that the firm's demise or attenuation would be deleterious to its customers in the area, including present and prospective institutional investors.[88/] As to Black, the Black Respondents urge that for over 20 years in the

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88/ The Black Respondents also strongly urge that the Division's proposed sanctions as to them are grossly out of proportion to other recommended sanctions and to sanctions imposed under settlements in this proceeding. The Commission has repeatedly held and the courts have confirmed that the remedial action which is appropriate depends on the facts and circumstances of each particular case and cannot be precisely determined by comparison with action taken in other cases. See, e.g., Transmittal Securities Corporation, Securities Exchange Act Release No. 9476, p. 4 (February 3, 1972); Hiller v. S.E.C., 429 F. 2d 856 (C.A. 2, 1970); Dlugash v. SEC., 373 F. 2d 107, 110 (C.A. 2, 1967).

securities business he has had an unblemished record[89/] and that as the president and largest owner and biggest producer in the firm his absence from the firm would adversely affect its fortunes and visit negative results upon innocent employees of the firm and on its actual or potential customers.

In consideration of all mitigating factors urged by the Black Respondents as well as others discussed above or disclosed by this record, it is considered that a 30 day suspension of Black together with a reprimand to Black Company would be adequate to satisfy, and best calculated to serve, the overall public interest. Black was the only active wrongdoer in the firm and his suspension for thirty days will inevitably have some negative impact on the firm, along with the reprimand and findings of violations that it will sustain. To attempt to revoke Black Company's registration for a period of time as respects institutional accounts only might do more harm to actual or potential institutional customers of the firm than the effort would be worth in terms of its deterrent effect.

As respects Pressprich, the essence of its dereliction is a failure adequately to supervise,[90/] which resulted in the single, isolated sale of one "hot" new issue to Pitt in 1966 by one of Pressprich's

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89/ Black Company has not prior to the events that are the subject of this proceeding been the subject of any disciplinary proceeding or action by any regulatory or self-regulatory body with the exception of one NASD proceeding relating to the firm's San Francisco office that resulted in a $700 fine.

90/ See pp. 38 and 42 and footnote 85, above.

Portland-office salesmen. The record indicates that Pressprich's compliance procedures, though not adequate, were generally equal to or superior to those then common to the industry, and that they have thereafter been strengthened. In light of all the mitigative factors urged by Pressprich or disclosed by this record, it is concluded that the findings of violations and of a failure to supervise against Pressprich will alone constitute sufficient deterrent effect and that accordingly it is not necessary to impose any sanction against Pressprich in the public interest.

ORDER

Accordingly, IT IS ORDERED as follows:

(1) Respondent Roy A. Pitt, Jr. is hereby barred from association with any broker or dealer with the proviso that after a period of nine months following the effective date of this Order he may apply to the Commission to become so associated in a non-supervisory, non-proprietary capacity upon a satisfactory showing to the Commission that he will be adequately supervised;

(2) Respondent Lawrence S. Black is hereby suspended from association with any broker or dealer for a period of one month following the effective date of this order: Provided, however, That this suspension shall not require Black to divest himself of his ownership interest in Black & Company, Inc. during the suspension period;

(3) Respondent Black & Company, Inc. is hereby censured, and

(4) The imposition of any sanction against R. W. Pressprich & Co., Inc. for its violations and failure to supervise is found not to be required or indicated in the public interest in view of the various mitigating circumstances found herein.

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

Pursuant to Rule 17(f), this initial decision shall become the final decision of the Commission as to each party who 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 not become final with respect to that party. 91/

David J. Markun
Administrative Law Judge

Washington, D.C.
July 12, 1974

91/ To the extent that the proposed findings and conclusions submitted by the parties, and the arguments made by them, are in accordance with the views herein they are accepted, and to the extent they are inconsistent therewith they are rejected. Certain proposed findings and conclusions have been omitted as not relevant or as not necessary to a proper determination of the issues presented.

APPENDIX A

APPENDIX A

REVISED CODE OF WASHINGTON ANNOTATED

Title 41

PUBLIC EMPLOYMENT

Chapters 41.28 to End

Title 42

PUBLIC OFFICERS AND AGENCIES

WITH FORMS

San Francisco, Cal.
Bancroft-Whitney Company

St. Paul, Minn.
West Publishing Company

CHAPTER 42.20

MISCONDUCT OF PUBLIC OFFICERS

Sections

CROSS REFERENCES

Agriculture department personnel, misconduct: RCWA 43.23.140.
Bribery and grafting: RCWA Chapter 9.18.
Bribery or corrupt solicitation prohibited: Const Art II § 30.
Cities and towns, commission form, misconduct of officers and employees: 35.17.150.
Cities, second class, misconduct of officers and employees: RCWA 35.23.230.
Code of ethics for public officers and employees: RCWA Chapter 42.22.
County commissioners misconduct relating to inventories: RCWA 36.32.220.
County officers, misconduct: RCWA 36.18.160, 36.18.170.
County sheriff, misconduct: RCWA 36.28.140.
County treasurer, suspension for misconduct: RCWA 36.29.090.
Election officials, misconduct: RCWA Chapter 29.85.
Extortion by public officer: RCWA 9.33.040.
False acknowledgment: RCWA 9.44.030.
Flood control district officers, interest in contracts prohibited: RCWA 86.05.590, 86.09.286.
Forfeiture of office upon conviction of felony or malfeasance: RCWA 9.92.120.
Free transportation for public officers prohibited: Const Art II § 39, Art XII § 20.
Irrigation districts, interest in contracts: RCWA 87.03.465.
Juries, misconduct of public officers concerning: RCWA Chapter 9.51.
Militia, misconduct: RCWA Chapter 38.32.
Oppression under color of office: RCWA 9.33.020.
Penitentiary employees, misconduct: RCWA 72.08.150, 72.08.160.
Personating public officer: RCWA 9.34.020.
Private use of public funds, penalty: Const Art XI § 14.

School funds, failure to turn over; RCWA 28A.87.080, 28A.87.130, 28A.87.135.
School officials,
Disclosing examination questions: RCWA 28B.60.070.
False reports: RCWA 28A.87.020–28A.87.050.
Granting: RCWA 28A.87.090.
School teachers,
Abuse of pupil: RCWA 28A.87.140.
Failure to display flag: RCWA 28A.02.030.
Failure to enforce rules: RCWA 28A.67.060.
State and judicial officers, impeachment: Const Art V.
State colleges of education, board of trustees, interest in contracts prohibited: RCWA 28B.40.120.
State treasurer, embezzlement: RCWA 43.08.140.
Township officers not to be interested in contracts: RCWA 45.16.110.

42.20.010 Misconduct of public officer. Every public officer who shall—

(1) Ask or receive, directly or indirectly, any compensation, gratuity, or reward, or promise thereof, for omitting or deferring the performance of any official duty; or for any official service which has not been actually rendered, except in case of charges for prospective costs or fees demandable in advance in a case allowed by law; or

(2) Be beneficially interested, directly or indirectly, in any contract, sale, lease, or purchase which may be made by, through or under the supervision of such officer, in whole or in part, or which may be made for the benefit of his office, or accept, directly or indirectly, any compensation, gratuity, or reward from any other person beneficially interested therein; or

(3) Employ or use any person, money, or property under his official control or direction, or in his official custody, for the private benefit or gain of himself or another;

Shall be guilty of a gross misdemeanor, and any contract, sale, lease or purchase mentioned in subdivision (2) hereof shall be void: *Provided,* That this section shall have no application to any person who is a state employee as defined in RCW 42.18.130.

LEGISLATIVE HISTORY

1. Enacted Laws 1909 ch 249 § 82 p 915. Based on:
(a) Code 1881 § 879.
(b) Laws 1873 p 200 § 83, Laws 1869 p 216 § 79, Laws 1859 p 119, § 74. Laws 1854 p 89 § 74.
2. Amended by Laws 1st Ex Sess 1969 ch 234 § 34 p 2266, adding the proviso at the end of the section.
See RRS § 2334.

CHAPTER 42.21

CODE OF ETHICS FOR PUBLIC OFFICIALS

Sections

CROSS REFERENCES

Executive conflict of interest act: RCWA Chapter 42.18.
Public officer, requiring or procuring bond or insurance on public works from particular insurer, broker, agent: RCWA 48.30.270.

42.21.010 Declaration of necessity and purpose. It is declared that high moral and ethical standards among public officials are essential to the conduct of free government; that a code of ethics for the guidance of public officials is necessary to prevent conflicts of interest in public office, improve standards of public service, and promote and strengthen the faith and confidence of the people of the state of Washington in their public officials.

LEGISLATIVE HISTORY

Enacted Laws 1st Ex Sess 1965 ch 150 § 1 p 224.

COLLATERAL REFERENCES

63 Am Jur 2d Public Officers and Employees §§ 262, 275 et seq., 309 et seq.
CJS Officers §§ 110–116.

Key Number Digests:
Officers ⇐110.

42.21.020 Definitions. "Public official" means every person holding a position of public trust in or under an executive, legislative or judicial office of the state and includes judges of the superior court, the court of appeals, and justices of the supreme court, members of the legislature together with the secretary and sergeant at arms of the senate and the clerk and sergeant at arms of the house of representatives, elective and appointive state officials and such employees of the supreme court, of the legislature, and of the state offices as are engaged in supervisory, policy making or policy enforcing work.

"Candidate" means any individual who declares himself to be a candidate for an elective office and who if elected thereto would meet the definition of public official herein set forth.

"Regulatory agency" means any state board, commission, department or officer authorized by law to make rules or to adjudicate contested cases except those in the legislative or judicial branches.

LEGISLATIVE HISTORY

1. Enacted Laws 1st Ex Sess 1965 ch 150 § 2 p 2244.
2. Amended by Laws 1971 ch 81 § 106, effective March 23, 1971, substituting "court, the court of appeals, and justices of the supreme court," for "and supreme courts," after "includes judges of the superior" in first sentence.

COLLATERAL REFERENCES

63 Am Jur 2d Public Officers and Employees § 1.
CJS Officers §§ 110–116.

Key Number Digests:
Officers ⇐110.

42.21.030 Prohibited practices—Using position to secure special privileges or exemptions. No public official shall use his position to secure special privileges or exemptions for himself, his spouse, child, parents or other persons standing in the first degree of relationship.

LEGISLATIVE HISTORY

Enacted Laws 1st Ex Sess 1965 ch 150 § 3 p 2245.

COLLATERAL REFERENCES

63 Am Jur 2d Public Officers and Employees §§ 280, 281.
CJS Officers §§ 110–116.

Key Number Digests:
Officers ⇐110.

42.21.040 ———Engaging in activities likely to require or induce disclosure of confidential information. No public official shall accept employment or engage in any business or professional activity which he might reasonably expect would require or induce him to disclose confidential information acquired by him by reason of his official position.

LEGISLATIVE HISTORY

Enacted Laws 1st Ex Sess 1965 ch 150 § 4 p 2245.

COLLATERAL REFERENCES

63 Am Jur 2d Public Officers and Employees §§ 275 et seq., 280, 281.
CJS Officers §§ 110–116.

Key Number Digests:
Officers ⇐110.

42.21.050 ———Disclosure of confidential information or use for personal benefit. No public official shall disclose confidential information gained by reason of his official position nor shall he otherwise use such information for his personal gain or benefit.

LEGISLATIVE HISTORY

Enacted Laws 1st Ex Sess 1965 ch 150 § 5 p 2245.

COLLATERAL REFERENCES

63 Am Jur 2d Public Officers and Employees §§ 280, 281.
CJS Officers §§ 110–116.

Key Number Digests:
Officers ⇐110.

42.21.060 Public officials and candidates to file statement concerning private interests. Every public official and such other public employees as may be provided for herein shall on or before January 31st of each year, and every candidate shall simultaneously with filing a declaration of candidacy, file with the secretary of state, a written statement of:

(1) The name of any corporation, firm or enterprise subject to the jurisdiction of a regulatory agency in which he has a direct financial interest of a value in excess of one thousand five hundred dollars: *Provided,* That policies of insurance issued to himself or his spouse, accounts in banks, savings and loan associa-

tions or credit unions are not to be considered financial interests; and

(2) Every office or directorship held by him or his spouse in any corporation, firm or enterprise which is subject to the jurisdiction of a regulatory agency; and

(3) The name of any person, corporation, firm, partnership, or other business association from which he receives compensation in excess of one thousand five hundred dollars during the preceding twelve month period by virtue of his being an officer, director, employee, partner or member of any such person, corporation, firm, partnership or other business association; and

(4) As to attorneys or others practicing before regulatory agencies during the preceding twelve month period, the name of the agency or agencies and the name of the firm, partnership or association of which he is a member, partner, or employee and the gross compensation received by the attorney and the firm, partnership or association respectively for such practice before such regulatory agencies; and

(5) A list of legal description of all real property in the state of Washington, in which any interest whatsoever, including options to buy, was acquired during the preceding calendar year where the property is valued in excess of fifteen hundred dollars: *Provided,* That legislators shall also comply with such rules or joint rules as they now exist or may hereafter be amended or adopted.

For the purposes of this section, and this section only, the Washington state personnel board, established by RCW 41.06.-110, shall adopt and promulgate rules and regulations in accordance with the standards and policies set forth in RCW 41.06.150, delineating which classified personnel employed by the state shall be required to complete and file the financial statement set forth in* sections 1 and 2 of this 1969 amendatory act, as they now exist or may hereafter be amended.

LEGISLATIVE HISTORY

1. Enacted Laws 1st Ex Sess 1965 ch 150 § 6 p 2245.

2. Amended by Laws 1st Ex Sess 1969 ch 188 § 1 p 144, (1) adding "such other public employees as may be provided for herein" after "Every public official and" in the first sentence; (2) substituting "simultaneously with" for "within thirty days after" after "every candidate shall" in the first sentence; (3) adding "five hundred" after "in excess of one thousand" in subd (1); (4) adding "accounts in banks, savings and loans associations or credit unions" after "his spouse" in the proviso in subd (1); (5) adding "and the gross compensation received by the at-

torney and the firm, partnership or association respectively for such practice before such regulatory agencies and" after "member, partner, or employee" at the end of subd (4); and (6) adding subd (5).

REVISER'S NOTE

"This 1969 amendatory act" [1969 1st ex. s. c 188] was an act containing only one section which section was the amendment to RCW 42.21.060 set forth above.

CROSS REFERENCES

Primary election candidates to file statement of purpose—Penalty: RCWA 29.18.140.

COLLATERAL REFERENCES

CJS Elections §§ 324, 334.

Attorney General's Opinions:

Ops Atty Gen 65-66 No. 44 (legislator who is attorney engaged in private practice of law as not required to report names of his client; period covered by first report that must be filed under this statute).

Ops Atty Gen 65-66 No. 69 (meaning of "public officials," "direct financial interest," and "regulatory agency").

Key Number Digests:

Elections ⇐309.

42.21.070 Annual report by secretary of state. On or before February 15th of each year, the secretary of state shall prepare a report containing the statements required to be filed pursuant to RCW 42.21.060, which reports shall be open to public inspection.

LEGISLATIVE HISTORY

Enacted Laws 1st Ex Sess 1965 ch 150 § 7 p 2246.

COLLATERAL REFERENCES

CJS States §§ 60 et seq.

Key Number Digests:

States ⇐73.

42.21.080 Penalty. Any person wilfully, knowingly and intentionally violating any provision of this chapter shall be guilty of a gross misdemeanor.

LEGISLATIVE HISTORY

Enacted Laws 1st Ex Sess 1965 ch 150 § 8 p 2246.

COLLATERAL REFERENCES

CJS Officers §§ 133, 147.

Key Number Digests:
Officers ⇐121.

42.21.090 Chapter inapplicable to state employees under executive conflict of interest act. This chapter shall have no application to any person who is a state employee as defined in RCW 42.18.130.

LEGISLATIVE HISTORY

Added by Laws 1st Ex Sess 1969 ch 234 § 36 p 2267.

CROSS REFERENCES

Executive conflict of interest act: RCWA Chapter 42.18.

CHAPTER 42.22

CODE OF ETHICS FOR PUBLIC OFFICERS AND EMPLOYEES

Sections

CROSS REFERENCES

Executive conflict of interest act: RCWA Chapter 42.18:
Misconduct of public officers: RCWA Chapter 42.20.

42.22.010 Declaration of necessity and purpose. It is declared that the high moral and ethical standards among the public servants are essential to the conduct of free government; that a code of ethics for the guidance of public officers and employees is necessary in order to eliminate conflicts of interest in public office, improve standards of public service, and promote and strengthen the faith and confidence of the people of Washington in their government.

LEGISLATIVE HISTORY

Enacted Laws 1959 ch 320 § 1 p 1555.

COLLATERAL REFERENCES

63 Am Jur 2d Public Officers and Employees §§ 262, 309 et seq.
CJS Officers § 103.

Key Number Digests:

Officers ⇐107.

42.22.020 Definitions. (1) State agency means any state board, commission, bureau, department, division, or tribunal other than a court.

(2) Legislative employee means any officer or employee of the legislature other than members thereof.

(3) Personal and private interest means any interest which pertains to a person, firm, corporation, or association whereby such person, firm, corporation, or association would gain a special benefit or advantage as distinguished from a general or public benefit or advantage.

(4) Confidential information means such information as is declared confidential by other specific statutes.

LEGISLATIVE HISTORY

Enacted Laws 1959 ch 320 § 2 p 1555.

COLLATERAL REFERENCES

63 Am Jur 2d Public Officers and Employees §§ 309 et seq.
CJS Officers § 103.

Key Number Digests:
Officers ⇐107.

42.22.030 Activities in conflict with discharge of duties prohibited. No officer or employee of a state agency or legislative employee shall have any interest, financial or otherwise, direct or indirect, or shall engage in any business or transaction or professional activity, or shall incur any obligation of any nature, which is in conflict with the proper discharge of his duties in the public interest.

LEGISLATIVE HISTORY

1. Enacted Laws 1959 ch 320 § 3 p 1555.
2. Amended by Laws 1961 ch 268 § 8, substituting "No officer or employee of a state agency or legislative employee" for "No officer, employee of a state agency, legislative employee, or other public official" at the beginning of the section.

COLLATERAL REFERENCES

63 Am Jur 2d Public Officers and Employees §§ 309 et seq.
CJS Officers § 103.

Key Number Digests:
Officers ⇐107.

42.22.040 Prohibited practices enumerated—Agency code of ethics. No officer or employee of a state agency, legislative employee, or other public officer shall use his position to secure special privileges or exemptions for himself or others.

(1) No legislative employee shall directly or indirectly give or receive or agree to receive any compensation, gift, reward,

or gratuity from any source except the state of Washington for any matter connected with or related to the legislative process unless otherwise provided for by law.

(2) No officer or employee of a state agency, or other public officer shall, directly or indirectly, give or receive or agree to receive any compensation, gift, reward, or gratuity from any source except the state of Washington, its political subdivisions, or employing municipal government, for any matter connected with or related to his services as such an officer or employee unless otherwise provided for by law.

(4) No person who has served as an officer or employee of a state agency shall, within a period of two years after the termination of such service or employment, appear before such agency or receive compensation for any services rendered on behalf of any person, firm, corporation, or association in relation to any case, proceeding, or application with respect to which such person was directly concerned and in which he personally participated during the period of his service or employment.

(5) No officer or employee of a state agency, legislative employee, or public official shall accept employment or engage in any business or professional activity which he might reasonably expect would require or induce him to disclose confidential information acquired by him by reason of his official position.

(6) No officer or employee of a state agency, legislative employee, or public official shall disclose confidential information gained by reason of his official position nor shall he otherwise use such information for his personal gain or benefit.

(7) No officer or employee of a state agency shall transact any business in his official capacity with any business entity of which he is an officer, agent, employee, or member, or in which he owns an interest.

(8) The head of each state agency shall publish for the guidance of its officers and employees a code of public service ethics appropriate to the specific needs of each such agency.

(9) No officer or employee of a state agency nor any firm, corporation, or association, or other business entity in which such officer or employee of a state agency is a member, agent, officer, or employee, or in which he owns a controlling interest, or any interest acquired after the acceptance of state employment, accept any gratuity or funds from any employee or shall sell goods or services to any person, firm, corporation, or association which is licensed by or regulated in any manner by the state agency in which such officer or employee serves.

LEGISLATIVE HISTORY

Enacted Laws 1959 ch 320 § 4 p 1556.

REVISER'S NOTE

Subdivision (3) of 1959 c 320 § 4 was vetoed.

COLLATERAL REFERENCES

63 Am Jur 2d Public Officers and Employees §§ 309 et seq.
CJS Officers § 103.

Attorney General's Opinions:

Ops Atty Gen 61-62 No. 5 (right of sheriff to receive reward offered by United States Post Office Department for performance of services instrumental to solution of crime relating to Postal Service).

Key Number Digests:

Officers ⇐107.

42.22.050 Sworn statement of relationship or interest in certain business entities required—Confidentiality. Each legislative employee, agency officer and such employees thereof as the agency head may by regulation provide, who is an officer, agent, member of, attorney for, or who owns an interest in any firm, corporation, association, or other business entity which is subject to state regulation shall file a sworn statement with the secretary of state disclosing the nature and extent of his relationship or interest, said statement to be kept in confidence and to be disclosed only to members of the legislature or any legislative committee which may be organized for the purpose of ascertaining a breach of this code, and the same also to be disclosed to any other authority having the power of removal of any public official or servant.

LEGISLATIVE HISTORY

Enacted Laws 1959 ch 320 § 5 p 1557.

COLLATERAL REFERENCES

63 Am Jur 2d Public Officers and Employees §§ 280, 281.
CJS Officers § 103.

Key Number Digests:

Officers ⇐107.

42.22.060 Chapter supplemental—Liberal construction. This chapter shall be construed liberally to effectuate its purposes and policy as set forth in RCW 42.22.010, and to supplement such existing laws as may relate to the same subject.

LEGISLATIVE HISTORY

Enacted Laws 1959 ch 320 § 6 p 1558.

COLLATERAL REFERENCES

Am Jur Statutes §§ 217 et seq.
CJS Officers § 103.

Key Number Digests:
Officers ⇐107.

42.22.070 Penalties. Any person violating any provision of this chapter shall be guilty of a gross misdemeanor, and such person may be removed from his position or office, in addition to any other remedies or penalties provided by law, as for misconduct or malfeasance in office.

LEGISLATIVE HISTORY

Enacted Laws 1959 ch 320 § 7 p 1558.

COLLATERAL REFERENCES

63 Am Jur 2d Public Officers and Employees §§ 346 et seq.
CJS Officers § 133.

Key Number Digests:
Officers ⇐121.

42.22.120 Chapter inapplicable to state employees under executive conflict of interest act. This chapter shall have no application to any person who is a state employee as defined in RCW 42.18.130.

LEGISLATIVE HISTORY

Added by Laws 1st Ex Sess 1969 ch 234 § 37 p 2267.

COLLATERAL REFERENCES

63 Am Jur 2d Public Officers and Employees §§ 280, 281.
CJS States § 113.

Key Number Digests:
States ⇐95.

APPENDIX B

APPENDIX B

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

August 11, 1952

In the Matter of THOMSON & McKINNON 11 Wall Street New York 5, New York and JACK KAHN (Securities Exchange Act of 1934 - Sections 15(b), 15A and 19(a)(3))	MEMORANDUM OPINION AND ORDER

These are private proceedings to determine whether from approximately January 1, 1946, to approximately February 10, 1951, Thomson & McKinnon ("registrant"), a partnership registered as a broker-dealer, and its employee, Jack Kahn, violated the anti-fraud provisions of the Securities Act of 1933 ("the Securities Act") and the Securities Exchange Act of 1934 ("the Exchange Act"), and the margin requirements of Section 7(a) of the Exchange Act, and, if so, whether it is necessary to impose remedial sanctions with respect to registrant's registration and its membership in the National Association of Securities Dealers, Inc. and on certain national securities exchanges.

Registrant and Kahn have in separate applications requested that our order of November 19, 1951, instituting these proceedings be amended to exclude from consideration by the Hearing Examiner in the preparation of his recommended decision and by us in our Findings and Opinion any transactions which occurred prior to

November 19, 1946. They contend that any transactions which occurred more than 5 years prior to the date of our order are barred from consideration by the statute of limitations set forth in Section 2462 of the Judicial Code which provides:

> "Except as otherwise provided by Act of Congress, an action, suit or proceeding for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise, shall not be entertained unless commenced within five years from the date when the claim first accrued if, within the same period, the offender or the property is found within the United States in order that proper service may be made thereon." 1/

It is contended that the phrase "an action, suit or proceeding" applies to administrative as well as judicial proceedings and that since neither the Securities Act nor the Exchange Act contains an applicable limitation period the instant proceedings are within the purview of the foregoing section. It is argued that the present proceedings relate to "the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise" because the sanctions which might be imposed are penalties within the meaning of the quoted section, and in this connection it is asserted that such a determination also would subject the respondents to the criminal penalties prescribed in Section 24 of the Securities Act and Section 32 of the Exchange Act for violations of those statutes.

The Judicial Code, which was revised in 1948, embodies the laws pertaining to the Federal courts, their jurisdiction and procedure, and nothing

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1/ 28 U.S.C. § 2462 (1948).

therein indicates that administrative proceedings are subject to its provisions.[1] On the contrary, the legislative history shows that administrative agencies subject to the requirements of the Administrative Procedure Act were not considered to be within the purview of its various provisions.[2] While this Commission exercises quasi-judicial functions in these proceedings, it does not by virtue of such activity exercise judicial functions within the meaning of the Federal Constitution and the Federal laws.[3]

1/ Senate Report No. 1559, 80th Congress, 2nd Session; House Report No. 308, 80th Congress, 1st Session.

Registrant attaches some importance to the use in Section 2462 of the word "proceeding" which did not appear prior to 1948 when the Judicial Code was revised. In our opinion the insertion of the word "proceeding" does not indicate any intent to enlarge the scope of Section 2462 to render it applicable to administrative proceedings. The word "proceeding" would appear to have been added to make the language of the section embrace all judicial litigation. In this connection it may be noted that a new provision, section 2461, added to the Code in the 1948 revision, inter alia, covers seizures and forfeitures of property and with respect to such actions speaks of "a proceeding by libel."

2/ In this connection it may be noted that it was proposed to incorporate provisions in the Judicial Code relating to the Tax Court for the purpose of making it a court of record and subjecting it as a judicial body to the provisions of the Code rather than leaving it as an administrative agency subject to the Administrative Procedure Act. 93 Cong. Rec. 6950-6959 (July 7, 1947).

3/ See Tracy v. Commissioner of Internal Revenue, 53 F. 2d 575 (C.A. 6, 1931); cert. den. 287 U.S. 632.

and, accordingly, is not bound by the rules of procedure which prevail in the courts.[1] In our view, therefore, Section 2462, relied upon by the respondents, has no applicability to these proceedings.[2]

The instant proceedings must accordingly be governed by the Exchange Act and by the Administrative Procedure Act, which together provide the applicable substantive and procedural rules. The Administrative Procedure Act, which was intended as a pervasive code of procedure for administrative agencies, contains no provision prescribing a period of limitation for administrative proceedings. While the Exchange Act does prescribe periods of limitation with respect to certain civil actions brought pursuant to the statute, it contains no provision limiting

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1/ Federal Communications Commission v. Pottsville Broadcasting Co., 309 U.S. 134 (1940); Goss v. Commissioner of Internal Revenue, 75 F. 2d 326 (C.A. 1, 1935).

2/ In view of this conclusion we need not consider the argument that the remedial sanctions provided for in the Exchange Act are "penalties" within the meaning of Section 2462 and that a determination that respondents have committed the alleged violations subjects them to criminal penalties. However we consider it appropriate to note that the sanctions which we may impose under the Exchange Act are not a penalty but are remedial in character, designed to protect investors and to prevent abuses in the future. Cf. Wright v. Securities and Exchange Commission, 112 F. 2d 89 (C.A. 2, 1940) where it was held that an expulsion order issued in a proceeding under Section 19(a)(3), which authorizes the Commission to suspend or expel a member from membership in a stock exchange, was not a punishment for past violations. Nor does the imposition of a remedial sanction of itself result in criminal penalties, which can be imposed only after a conviction in judicial proceedings.

the time within which this Commission must institute proceedings for remedial action in the public interest for the purpose of carrying out the duties entrusted to it by Congress. The absence of any prescribed period of limitation in either of these Acts for the institution of remedial administrative proceedings is consistent with the statutory pattern of authorizing this Commission to initiate appropriate administrative action when necessary to safeguard the public interest and the interests of investors, the objectives of the Exchange Act.

Accordingly, IT IS HEREBY ORDERED that the applications of Thomson & McKinnon and Jack Karn to amend the order instituting proceedings pursuant to Sections 15(b), 15A and 19(a)(3) of the Securities Exchange Act of 1934 be, and they hereby are, denied.

By the Commission (

Orval L. DuBois
Secretary