ADMINISTRATIVE PROCEEDING
FILE NO. 3-326

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of

KENNEDY, CABOT & CO., INC.
DAVID PAUL KANE
LINDA D. TALLEN

(8-8621)

INITIAL DECISION

(Private Proceedings)

Sidney L. Feiler
Hearing Examiner

Washington, D. C.
August 27, 1968

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APPEARANCES: Messrs. Robert M. Berson, Joseph C. Daley, and D. J. Silman, for the Division of Trading and Markets

Clark van der Velde, Esq., 1930 Century Park West, Los Angeles, California 90067, for Kennedy, Cabot & Co., Inc. and David Paul Kane

George J. Nicholas, Esq., Nicholas Building, 1532 3rd Street, Santa Monica, California, 90401, for Linda D. Tallen.

BEFORE: Sidney L. Feiler, Hearing Examiner

I. THE PROCEEDINGS

These are proceedings instituted by order of the Commission pursuant to Section 15(b) of the Securities Exchange Act of 1934, as amended ("Exchange Act") to determine whether certain allegations set forth in the order are true and, if so, what, if any, remedial action is appropriate in the public interest pursuant to Section 15(b) of the Exchange Act.

The matters put in issue by the allegations in the order as amended are:

A. Whether during the period from approximately June 1960 to approximately December 1962 Kennedy, Cabot & Co., Inc. (referred to herein as "registrant" or "K. C. & Co."), David Paul Kane, a person in control of the operations of the registrant at all relevant times, and Linda D. Tallen, a registered representative of the registrant, willfully violated Sections 5(a) and (c) of the Securities Act of 1933, as amended, ("Securities Act") in that they directly and indirectly made use of the means and instruments of transportation and communication in interstate commerce and of the mails to offer for sale, sell and deliver after sale and to offer to buy the common stock of American States Oil Company ("ASO") when no registration had been filed or was in effect as to such securities under the Securities Act.

B. Whether during the aforementioned period the above respondents, singly and in concert, and while engaged in the alleged

violations of Section 5 of the Securities Act willfully violated and willfully aided and abetted violations of Section 10(b) of the Exchange Act and Rule 17 CFR 240.10b-6 thereunder in that said persons, by themselves and with others, directly and indirectly bid for and purchased ASO securities for accounts in which they had a beneficial interest and attempted to induce others to purchase such securities prior to the time said persons had completed their participation in such distribution.[1/]

C. Whether, during the period aforementioned, K.C. & Co., Kane, Tallen, and two former registered representatives of registrant, Fred J. Prince[2/] and Julian F. Fleg,[3/] singly and in concert, willfully

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1/ Under the cited provisions the activity of a broker or other person who has agreed to or is participating in a distribution of securities in bidding for or purchasing for any account in which he has a beneficial interest, any security which is the subject of such distribution, until after he has completed his participation in such distribution constitutes a "manipulative or deceptive device or contrivance" prohibited by the Exchange Act.

2/ Prior to the hearing herein Prince filed a stipulation and consent to findings that he had willfully violated and willfully aided and abetted violations of the Securities Acts. He also consented to an order imposing sanctions against him. (Fred J. Prince, Sec. Exch. Act Rel. No. 7781, January 4, 1966).

3/ Shortly after the hearing herein commenced the Commission accepted an offer of settlement submitted on behalf of Fleg pursuant to which Fleg consented to the entry of an order finding that he committed willful violations as alleged in the order for proceedings and further consented to the imposition of sanctions against him. (Julian F. Fleg, Sec. Exch. Act Rel. No. 8105, June 23, 1967.)

violated and willfully aided and abetted violations of the anti-fraud provisions of the Securities Acts[4/] in the offer, sale and purchase of ASO securities by certain described activities, by inducing persons to purchase and selling to such persons ASO securities at prices which, under the circumstances, were excessive and unreasonable; making untrue, deceptive and misleading statements of material facts and omissions to state material facts concerning, among other things, the ownership of certain tidelands oil leases, the ownership and economic potential of certain oil leases in Oklahoma and the status of drilling operations on these leases; the income and assets of ASO; the value of ASO stock; the present and future market price of ASO stock; the listing of ASO stock on a national securities exchange; and the use of proceeds from the sale of ASO stock.

Pursuant to notice, a hearing was held at Los Angeles, California with all parties being represented by counsel. At the conclusion of the presentation of evidence, opportunity was afforded the parties for filing proposed findings of fact and conclusions of law, together with

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4/ Section 17(a) of the Securities Act and Sections 10(b) and 15(c)(1) of the Exchange Act and Rules 10b-5 and 15c1-2 (17 CFR 240.10b-5 and 15c1-2) thereunder are sometimes referred to as the anti-fraud provisions of the Securities Acts. The composite effect of these provisions, as applicable here, is to make unlawful the use of the mails or interstate facilities in connection with the offer or sale of any security by means of a device or scheme to defraud or untrue or misleading statements of a material fact, or any act, practice, or course of conduct which operates or would operate as a fraud or deceit upon a customer or by means of any other manipulative or fraudulent device.

briefs in support thereof. Proposed findings, together with supporting briefs, were submitted on behalf of all the parties.

II. FINDINGS OF FACT AND LAW

A. The Registrant

Kennedy, Cabot & Co., Inc. became effectively registered as a broker-dealer pursuant to provisions of Section 15(b) of the Exchange Act in June 1960, and such registration is still in effect. At all times here relevant it maintained offices in Beverly Hills, California. David Paul Kane is president and owner of more than 10% of the common stock of registrant. Linda D. Tallen was the secretary of registrant from approximately January 18, 1961 to approximately December 18, 1961. She also has been a registered representative of registrant since December 1960.

Roland H. Brocking was the trader for registrant until the end of February 1961. Thereafter, Kane and Tallen conducted trading activities for the registrant. The registrant's staff consisted of a few full-time employees, perhaps no more than three or four at any time, supplemented by some part-time employees who were selling mutual funds.

B. Violations of the Registration Provisions of the Securities Acts

1. History of ASO, its Capitalization, Issuances of Its Stock, and Control of ASO by J. Tom Grimmett

ASO was incorporated on May 6, 1952. Its stated purpose was to deal in real property and prospecting, developing and dealing

in oil, gas and minerals.

ASO made two filings with the Commission for its securities. On May 28, 1952 it filed a notification under Regulation A with the Commission covering 575,000 shares of its common stock at 50¢ per share. This offering according to company reports was sold.

On August 10, 1954 ASO and J. Tom Grimmett as selling stockholder filed a notification under Regulation A covering a proposed offering of an indeterminate number of shares of common stock with a par value of 10¢ per share with the aggregate offering price and market value not to exceed $50,000. On November 21, 1956 the Commission issued an order temporarily suspending the Regulation A exemption. No registration statement was ever filed by ASO with the Commission.

At all times here relevant Grimmett was a person in control of ASO. He was one of the company's three original incorporators and was president from 1952 to November 15, 1954. According to ASO's corporate minutes he was ASO's principal stockholder at that time and guaranteed all future financing for the company. The reason given for his resignation was that he was ASO's principal creditor.

Grimmett continued to serve as a director of ASO from November 15, 1954 until June 30, 1959 when he was re-elected president of ASO. From 1952 to at least June 1959 Grimmett financed ASO's operations primarily from sales and pledges of his personally-owned ASO stock. On July 24, 1956 in an action instituted by the Commission, Grimmett was personally enjoined by order of the United States District

Court for the Southern District of New York from further violating the registration provisions of the Securities Act in the sale of shares of stock of ASO. This final judgment was obtained on allegations in affidavits filed in support of the Commission's complaint that Grimmett had received 5,391,666 of ASO's authorized 6,000,000 shares and had sold and disposed of approximately 4,000,000 shares of his personally-owned stock. (Div. Ex. 9-C).

The aforementioned order of the Commission on November 21, 1956 temporarily suspending the exemption for the sale of ASO stock was based on allegations that ASO and Grimmett had failed to disclose the sale of a substantial number of unregistered shares of ASO by Grimmett within one year prior to the filing of a notification, that the aggregate price of all of the issuer's stock sold by Grimmett substantially exceeded permissible amounts, and the existence of the aforementioned injunction issued against Grimmett. (Div. Ex. 8, 9-B).

Despite the existence of the aforementioned court order certain steps were taken by Grimmett commencing in June 1959 and under his direction, which resulted in a substantial distribution to the public of unregistered shares of ASO. Grimmett resumed the presidency of ASO in June 1959 and continued as such until his death in 1964. Grimmett's brother-in-law was substituted as a new transfer agent. Prior to June 30, 1959 ASO had authorized 6,000,000 shares of 10¢ par value stock of which 5,996,666 were issued and outstanding. On June 30, 1959, a reverse split of 20 for 1 was authorized by

shareholders so that a total of 299,833 and 6/20 shares of new $2 par value stock was issued and outstanding as of that date; there being an authorized capitalization of 3,000,000 such shares. The same day the directors of ASO, with shareholder approval, authorized the issuance of 650,000 shares of ASO stock to the Pauls Valley National Bank ("PVNB") as escrow agent and trustee for Grimmett. These shares were issued and delivered to PVNB in July 1959 and were held by that bank. At all relevant times Grimmett's brothers were officers of this bank.

On September 25, 1959 the directors authorized the issuance of an additional 550,000 shares of ASO stock to Grimmett or his nominee. In October and November 1959, and in January 1960, these shares were issued to Mid-State Drilling Co. ("Mid-State"), a nominee for Grimmett. Larry Gulihur, Grimmett's son-in-law, was nominal president of Mid-State but worked for Grimmett and took directions from him. As of January 1960 there were a total of 1,499,833-6/20 shares of ASO stock issued and outstanding and there were no additional original issuances of stock thereafter.

2. Distributions of ASO Stock by Grimmett and Mid-State

Mid-State had been used as a vehicle for transactions between ASO and Grimmett over a period of years. In January 1956 ASO acquired Mid-State from two individuals for the sum of $7,500 and 20,000 shares of ASO stock. In March 1957 Grimmett obtained all the shares of

Mid-State from ASO for the purported consideration of $15,000 in the form of a reduction of ASO's debt to him. At that time according to the records, Mid-State had no assets whatsoever as all its leases had expired. (Div. Ex. 47).

In 1957 Grimmett appointed Gulihur president of Mid-State. At that time the stock of Mid-State was nominally held by Gulihur, his wife, and his mother-in-law. During the period from 1957 through 1961 Gulihur performed secretarial services for Grimmett and ASO, was paid by Grimmett, and did not receive any income from Mid-State. From 1957 through 1961 while Gulihur was president of Mid-State it did not maintain any books and records of its own other than a checkbook and documents relating to the checkbook. All other books and records of Mid-State were combined with the personal books and records of Grimmett.

Part of Grimmett's substantial holdings in ASO were acquired under the following conditions: the 650,000 shares of ASO stock issued to PVNB in July 1959 for him were in consideration of the acquisition by ASO of a one-half interest in certain water flood property in Nowata County, Oklahoma,owned by Grimmett. The other large block of 550,000 shares of ASO stock issued to Mid-State as Grimmett's nominee were in consideration of the acquisition by ASO from him of the remaining one-half interest of the water flood property aforementioned. This transaction was authotized on September 25, 1959. During the period from approximately August 1960 through July 1961 Mid-State also purchased

a total of more than 100,000 shares of ASO stock in the open market through various broker-dealers.

Commencing in the summer of 1959 and continuing through December 1962 Grimmett through Mid-State and Gulihur offered, sold and delivered after sale a total of 609,467 shares of ASO stock. Of these shares 505,000 were part of the block of 550,000 shares of ASO stock issued to Mid-State in the 1959 recapitalization of ASO. (Div. Ex. 49-C). Mid-State realized approximately $680,500 from sales from this block. By September 1961, it was the record owner of only 66,900 shares remaining from its total holdings.

One of the conduits through which Grimmett effected distribution of stock to the public was Honnold & Co., a broker-dealer firm in Oklahoma City. From 1959 through 1961 Honnold sold 36,700 shares of ASO stock for Grimmett, at least 34,700 of which were part of the 550,000 shares issued to Mid-State. The procedure used was that whenever Honnold received an order it was filled by stock supplied by the PVNB which in turn received the stock from Mid-State and sight-drafted it to the broker-dealers' correspondent bank.

3. Transactions by K.C. Co. in ASO Stock

From January through June 1961 registrant purchased as principal 9200 shares of ASO stock from Honnold, of which at least 7200 emanated from the block of 550,000 shares issued to Mid-State. This stock in turn was offered and sold by registrant to its customers. There were three such transactions at a total price of $39,100.

From January through October 1961 registrant purchased 9,930 additional shares of ASO stock from sources other than Honnold. Its largest transactions were with D. H. Blair & Co. from whom it purchased at least 5,550 shares of stock in ten transactions. These shares were sold out of the account of Gulihur who was acting as nominee for Mid-State and Grimmett.[5/] Its sales to broker-dealers and customers from January 30, 1961 through September 1, 1961 totalled 17,200 shares. Registrant's original purchases of ASO stock were effected by Brocking as its trader. On February 6, 1961 and on February 15, 1961 blocks of 1,000 shares each were purchased from Honnold and subsequent purchases of ASO stock were effected by either Tallen or Kane. Tallen played the dominant role in retail sales to customers of registrant.

4. Relationship of Tallen to Grimmett; Tallen's Transactions in ASO Stock

Tallen and Kane had business dealings with Grimmett prior to their activities in the purchase and sale of ASO stock. In 1959, Tallen was the part owner of a womens' health club known as "Fair Lady." Kane held a minority interest. In the fall of that year Grimmett was introduced to Tallen as a prospective buyer of Fair Lady and after some negotiations during which Tallen became aware that Grimmett was

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5/ There was extensive trading in ASO stock in this account; 104,126 shares were received into it and 136,888 were delivered out from November 11, 1960 to July 14, 1961. Purchases were made from thirty-eight broker-dealers (K.C.Co. 2,000 shares) and sales were made to eighteen firms, including registrant. As of May 1961 there was a debit balance in this account of $147,502.23.

in the oil industry and was connected with ASO an agreement was worked out by which Grimmett agreed to purchase Fair Lady and an adjoining parking lot. He gave Tallen a post-dated check for $30,000 as part of this sale, which check was not honored. A new arrangement was entered into in January 1960 under which Grimmett took possession of Fair Lady, making no down payment, but agreeing to complete the purchase in six months. At that same time Tallen learned that Grimmett was president of ASO and its largest stockholder. Grimmett did not complete his purchase of Fair Lady and Kane arranged for the sale of that business to a third party in August 1960. During the period from January to September 1960, according to Tallen, she loaned Grimmett sums of money aggregating approximately $40,000.

Kane had known Tallen for a substantial period of time prior to their association at Fair Lady. After Fair Lady was sold in August 1960 Kane and Tallen discussed an arrangement whereby Tallen would become associated with the registrant. An agreement was therefore made under which Tallen became associated with the registrant and was to receive reimbursement for expenses.[6/] Tallen became formally associated with the registrant in December 1960 when she became a registered representative. A month later she became an officer of registrant and was in charge of K. C. Co. when Kane went abroad.

6/ The books of registrant, however, note commission payments to her in 1961 of $5,144.65 (Div. Ex. 43A).

Tallen had meetings with Grimmett in the fall and winter of 1960. She testified she made repeated efforts without success to obtain payment for the loan she had made to Grimmett. In November 1960 he urged her to take ASO stock in payment of his debts to her. She refused. Tallen knew from Grimmett that Gulihur was an officer of Mid-State and that Gulihur, his wife and mother-in-law owned Mid-State and that Mid-State traded certain properties for ASO stock.

In December 1960 Grimmett gave Tallen two checks drawn on his account at PVNB for $17,500 and $3,530.20. These checks were not honored. In February 1961 Tallen agreed to accept 5,000 shares of ASO stock in reduction of part of the debt owed her by Grimmett. She knew at that time from Grimmett that he could not sell his personally owned stock because it was "locked up" at PVNB and was watched by SEC representatives. Grimmett told Tallen that Gulihur would give her ASO stock belonging to Mid-State and on March 10, 1961 Gulihur mailed her such a stock certificate. In May 1961 Tallen agreed to accept another 2,500 shares of ASO stock, plus $4,200 in cash in liquidation of the remaining sum that Grimmett owed her. She received a certificate from Mid-State.

In July 1961, Tallen was involved in two loan transactions in which Grimmett, Paul P. Gelles 7/ and Gulihur each played a part. According to Tallen, in the early part of July Grimmett telephoned

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7/ Gelles was a customer of K. C. Co. Tallen had sold him some ASO stock and had introduced him to Grimmett.

her and told her that he needed 4 or $500,000 for oil properties and asked her to have Gelles call him. Tallen passed on the message and later lunched with Gelles who told her that he understood Grimmett's position. He later told her that he was going to arrange a loan for Grimmett of $100,000 (Tr. p. 1539, et seq.). He also told her that Grimmett had promised him options and that he had asked Grimmett to call him back because he wanted to call some of his friends and see if he could place the stock.

A few days later Gelles asked Tallen to pick up Gulihur at the Los Angeles airport. Gulihur told her that he had with him 100,000 ASO shares which Gelles or Grimmett had told him to put in her name. The morning of July 10 Tallen went with Gelles to a bank where she signed papers pledging the 100,000 shares as collateral for a loan in the sum of $100,000 guaranteed by Gelles. A check in that amount made out to the clearing broker for the Blair firm in New York was given to Gelles. This check was subsequently remitted and used as a payment into an account maintained by Gulihur in which he was trading substantial amounts of ASO stock. After the loan had been made Gelles, Gulihur and Tallen went to Tallen's attorney and an agreement was prepared by counsel and signed by Gelles and Tallen. This agreement, predated July 8, 1961, specified that the parties thereto agreed to participate on a 50/50 basis in the acquisition of 50,000 shares of ASO stock which were then part of the pledged collateral for the bank loan. They also agreed that any losses that might result because of the bank loan would be shared on a 50/50 basis (Tallen

Exhibit 14).[8/] Tallen was reimbursed with a Mid-State Drilling Co. check for her legal expenses incurred at the July 10, 1961 meeting with her counsel. The aforementioned agreement mentioned that the stock had been placed in Tallen's name as a matter of convenience only and that she had acted as agent. Default was made on the repayment of this loan and Tallen later endorsed the certificates so that efforts could be made to recoup the balance due.

On July 25, 1961 Gelles and Tallen went to a bank to arrange for loans to each of $50,000. Tallen testified that she was talked into making this loan by Gelles who thought it would be a good idea to borrow the money to exercise an option to buy 25,000 more ASO shares because "his brokers were selling it at astronomical figures."[9/] The purchase was going to be made the following day from Gulihur. Tallen did receive a loan for $50,000 guaranteed by Gelles. Tallen further testified that when her attorney raised objections to the transaction she returned the money to the lending bank and went no further in the proposed transaction. Bank records indicate that the purpose of the loan to Tallen was stated as "Investment in Unlisted Stock Amer States Oil with Paul Gelles." (Division Exhibit 90-G). Gelles used the proceeds of his loan to obtain ASO

8/ Gelles also signed an instrument stating that in consideration of the indemnification arrangement that Tallen had entered into he was assigning 50% of certain option rights he had acquired.

9/ Division Exhibit 140, pages 254-260, 311.

stock from Gulihur. Prior to returning the check, Tallen, according to her testimony, told Gulihur, Grimmett and Gelles what she intended to do.[10/] She also testified that she heard Gelles tell Grimmett that he was going to syndicate stock from Grimmett through other brokerage firms (Tr. 1916). She found out in August from other brokers that he was making such efforts:[11/]--

As previously noted Tallen personally received 7,500 shares of ASO stock in accordance with an arrangement she made with Grimmett and in partial satisfaction of the debt that he owed her. Tallen maintained that she had loaned Grimmett approximately $40,000 prior to July 1961 and the stock she received plus cash payment of $4,200 was in satisfaction of that debt. Subsequently, according to her testimony she loaned Grimmett an additional $15,000 to pay some expenses in developing Long Beach oil property.

The shares of ASO stock which Tallen received emanated from the 550,000 shares issued to Mid-State by ASO. Tallen received one certificate for 5,000 shares on or about March 10, 1961 and a second certificate for 2,500 shares in May 1961. This latter certificate was mailed from Mid-State directly to registrant and was then

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10/ Tallen received a note of indemnification from Gulihur dated July 26, 1961, endorsed by Grimmett, as to her liability on her July 8 agreement with Gelles.

11/ Later, there was litigation between Gelles, on the one hand, and Grimmett, Gulihur and Tallen over Gelles' transactions in ASO stock. This litigation was never completed because of the death of Gelles during the pendency of the proceeding.

delivered by it to Tallen.

On August 8, 1961 Tallen delivered this latter certificate to the registrant. From it, on August 14, 1961 she sold registrant 600 shares. The next day she sold registrant an additional 500 shares. In the final transaction, on October 25, 1961 Tallen sold an additional 200 shares to registrant. Tallen received from the registrant a total of $3,600 for her sale of 1,300 shares of ASO stock to it.

Tallen also was instrumental in effecting transactions in ASO stock which were not reflected on the books and records of K. C. & Co. On January 11, 1961 Tallen offered and sold Paul Chernow 2,000 shares of ASO stock at $3 a share. Chernow gave Tallen a cashier's check and subsequently received certificates from Mid-State which were part of the 550,000 share block of ASO stock previously issued to Mid-State as Grimmett's nominee. In March 1961 Tallen arranged for Chernow to purchase an additional 2,000 shares. His certificates for this transaction also emanated from the 550,000 share block of ASO stock.

On or about March 15, 1961 Tallen offered and sold Jay Etkin, a K. C. & Co. representative, 100 shares of ASO stock at $5 a share. She told him that this stock was coming directly from the president of ASO. Etkin gave Tallen a check with the payee's name left blank. Mid-State's name was stamped on the check later and Gulihur endorsed it.

Ronald H. Brocking, registrant's trader until the end of February 1961, testified that Tallen participated in an arrangement whereby he agreed with Grimmett to buy 500 shares of ASO stock. The testimony of Brocking impressed the undersigned as reflecting animus toward Tallen and Kane and the undersigned has not given it any weight in the findings herein.

5. Contentions of the Parties as to Tallen's Activities - Conclusions

It was clear that Grimmett, a person in control of ASO, through Mid-State and by various devices, was engaged in a very substantial distribution of unregistered ASO stock at all times here relevant. While conceding that there was such activity and that Tallen participated in it, it is urged on her behalf that she unknowingly violated Sections 5(a) and (c) of the Securities Act and did not do so willfully as alleged in the order for these proceedings. It is argued that Tallen was not aware that the ASO shares that registrant was obtaining from Honnold actually emanated from Mid-State and were part of an unregistered distribution. It is also contended that Tallen was unaware of the exact relationship between Grimmett and Gulihur prior to July 1961 and did not know of Grimmett's prior activities in ASO stock and the injunction outstanding against him.

With reference to her participation in transactions involving Gelles and not passing through the registrant's books, ~~with respect to Chernow transactions~~, these, it is asserted, involved arrangements between Gelles, an acknowledged sophisticated and wealthy investor, and Grimmett. Tallen's participation, it is urged, was that of an unwilling conduit

pressured into her participation only after having received advice of counsel that the transaction was completely proper. Finally, it is asserted that Tallen terminated all her activities and associations with Grimmett, Gelles, and Mid-State on or about July 26, 1961, when she returned a loan she had obtained from the Fidelity Bank and told Grimmett, Gelles and Gulihur, according to her testimony, that she did not want to have anything more to do with them. It was also pointed out that sales made to investors by Tallen through the registrant were approximately 1% of the 600,000 shares sold during the period involved.

It is argued that any violations that were made were not willful because Tallen did not know or had no reason to know that her conduct violated Section (5) of the Securities Act. Tallen, it is pointed out, had very little experience in the securities business at the time initial trades were made in ASO stock and that the trader, Ronald H. Brocking, had been in the securities business since 1945 and had advised Tallen and Kane that good houses were making a market in ASO and therefore it would be proper for registrant to effect transactions therein.[12/]

Certain aspects of Tallen's dealings in ASO stock are very clear from the record. She knew, even prior to her association with the registrant, that Grimmett was the president of ASO and in control

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12/ Brocking testified that the initial trades by registrant and ASO stock were made at the behest of Tallen. For the purpose of evaluating Tallen's conduct, her version is accepted.

of its operations. While he told her, according to her testimony, that his personally owned stock was "locked up" and could not be touched by him he urged her to accept ASO stock from him in settlement of his debt to her. As early as January 1961 she remitted money to Mid-State for stock in payment for purchases in which Grimmett had played a part. She received stock from Mid-State after she had negotiated an arrangement with Grimmett to accept ASO stock in partial payment of Grimmett's debt to her. Her second certificate also came from Mid-State, yet she apparently made no effort during this period to try to ascertain Grimmett's connection with Mid-State or why ASO stock was readily available from it in large blocks. In July when she participated in the $100,000 loan transaction the relationship among Grimmett, Mid-State and Gelles was obvious. They were engaged in a transaction whereby money would be raised to meet substantial obligations in a Grimmett-controlled brokerage account where a large amount was due and owing for transactions in ASO stock. At the same time,by option arrangements and other devices, a large block of unregistered ASO stock was to be funnelled to Gelles and Tallen for distribution on the West Coast.

It is asserted on Tallen's behalf that she entered into the loan transaction because she was told by the other parties that if she did not do so the stock would drop to 10¢ a share. This does not excuse her participation in an arrangement so clearly violative of the public's right to be protected by the registration provisions of the Securities Act. While it also is asserted that Tallen relied

upon advice of counsel in entering into the loan transaction, the evidence indicates that the agreement that she entered into was signed after the loan itself had been made. Furthermore, the document itself does not purport to be a legal opinion as to the validity of Tallen's transactions from the standpoint of the provisions of the Securities Act nor is there any indication that it was based in any part on consideration of all of Tallen's other activities and transactions in ASO stock. Finally, the Commission has noted that reliance upon the advice of counsel does not negate either the Commission of a violation of the Securities Acts or willfulness.[13/]

Counsel relies upon U. S. v. Crosby, 294 F. 2d 928 (C.A. 2, 1961) on the issue of willfulness. The Crosby case was a criminal case where the elements of violation are different from those in an administrative proceeding. The Commission has pointed out in a long series of cases that a finding of willfulness under the Securities Acts does not require that there be a finding of an intent to violate, but merely an intent to do the acts which constitute a violation.[14/]

13/ Dow Theory Forecast, Inc., Investment Advisers Act Rel. No. 223, p. 10 (July 22, 1968); Gearhart & Otis, Inc., Sec. Exch. Act Rel. No. 7329, p. 34 (June 2, 1964), aff'd 348 F. 2d 798 (C.A.D.C. 1965). Strathmore Securities, Inc., Sec. Exch. Act Rel. No. 8207, p. 8 (Dec. 13, 1967).

14/ Tager v. S.E.C., 344 F. 2d 518 (2nd Cir. 1965); Harry Marks, 25 S.E.C. 208,220 (1947); George W. Chilian, 37 S.E.C. 384 (1956); E. W. Hughes & Company, 27 S.E.C. 629 (1948); Hughes v. S.E.C., 174 F. 2d 969 (C.A. D.C.,1949); Shuck & Co., 38 S.E.C. 69 (1957); Carl M. Loeb, Rhoades & Co., 38 S.E.C. 843 (1959); Ira Haupt & Company, 23 S.E.C. 589, 606 (1946); Van Alstyne, Noel & Co., 22 S.E.C. 176 (1946); Thompson Ross Securities Co., 6 S.E.C. 1111, 1122 (1940); Churchill Securities Corp., 38 S.E.C. 856 (1959); Gilligan,Will & Co., 38 S.E.C. 388, 395 (1958), aff'd 267 F. 2d 461 at p. 468 (1959), cert. denied 361 U.S. 896 (1959).

Tallen maintained that she did not know that K.C. & Co. was acquiring stock through Honnold from the Mid-State portfolio. For most of the period involved here she shared trading duties with Kane and also was an officer of the registrant. Her dealings with Grimmett and her acquisition of stock certificates from Mid-State should have alerted her at least to the possibility that stock of this little known company which was coming on the market in such substantial amounts ought to be carefully checked for possible violations of the registration provisions of the Securities Act. A securities salesman, and Tallen had a more responsible position with registrant, is not free to ignore the possibility that violations of the registration provisions may be taking place in a security he is selling when there are suspicious circumstances.[15/] The undersigned concludes that there were such circumstances here which Tallen at the very least ignored.

The undersigned concludes that Tallen by her activities set forth above willfully violated the registration provisions of Section 5 of the Securities Act.

6. Activities of Registrant and Kane in the Purchase and Sale of ASO Stock at K.C. & Co.

Kane testified that he first heard about ASO in November 1960 when Philip Honnold of Honnold and Co. came to the registrant's office and mentioned it in the course of a general conversation.

15/ Strathmore Securities, Inc., supra, p. 8; Langley-Howard, Inc., Securities Exchange Act Release No. 8361, p. 7 (July 25, 1968)

Registrant's records showed that it made a sale of 400 shares for a customer on December 5, 1960. Its first sale to a customer was on January 16, 1961. Its first purchase was on January 13, 1961 when it purchased 130 shares from a broker. (Division Exhibit 54). Kane left for a trip to Europe about the middle of January 1961 and did not return until the end of February. He testified that he told Tallen and Ronald Brocking, his trader, that he did not want any stock put into inventory. Despite this instruction, 1,000 shares were purchased from Honnold on February 6 and an additional 1,000 were purchased on February 15. Both Brocking and Tallen each stated that the other had taken the initiative in these shares. Brocking's father-in-law did purchase 200 shares from this block.

When Kane returned he discharged Brocking for violation of his instructions. Prior to the discharge Brocking had told him, he claimed, that he had positioned the stock because he thought it would be a good investment for registrant, that he had made a study of ASO, that reputable firms were listed in the quotation sheets for the stock and this meant that they had fully researched it and were satisfied to offer it, and that he knew and had spoken with traders for some of those firms about the stock.

Kane denied that he had had any discussions with Grimmett about ASO and asserted that neither he nor the registrant had anything to do with Tallen's transactions with Gelles in July 1961 and that he only learned of these transactions after Tallen had decided to take

back the check for $50,000 in a loan transaction with the Fidelity Bank, previously referred to. He also stated that he criticized Gelles for entering into the loan transactions with her.

Kane knew that Grimmett owed Tallen money as a result of loans made by her to Grimmett. He further testified that Tallen and Brocking told him on his return from Europe that Mid-State Drilling Co. was a company that owned a considerable amount of ASO stock. Thereafter, registrant continued to buy stock to fill orders written by its salesmen, and Kane, according to his testimony, continued to rely in part on the continued listing of good brokerage houses quoting the stock in the quotation sheets. He also stated that he did not make any check to see if ASO had a registration statement on file with the Commission because of the brokerage houses listed as selling it. He never learned of the Commission actions involving ASO stock and Grimmett. He further testified that he knew that stock obtained from Honnold came from PVNB, that he knew that Mid-State had ASO stock and that registrant had received some of their holdings but denied knowing the amount of stock they had or any relationship between Mid-State and ASO. He denied any knowledge of the relationship between Mid-State, ASO and Grimmett and also maintained that he did not know that the stock purchased from Honnold was attributable to Grimmett or Mid-State. He asserted he never met Gulihur in 1961 nor did he know that the stock sold by Tallen through K. C. & Co. emanated from Grimmett.

Contentions of the Parties; Conclusion

It is asserted on behalf of the registrant and Kane that neither Kane nor the registrant knew or had reasonable cause to know that Grimmett controlled Mid-State nor did they know that stock purchased from Honnold or other brokers was attributable to either Mid-State or Grimmett and that in the absence of such knowledge neither registrant nor Kane can be deemed to have violated Section 5 of the Securities Act. Reliance is also placed on the fact that at the time that K. C. & Co. effected transactions in ASO stock ASO shares were being actively traded with brokerage houses of excellent repute, that none of such firms disclosed they were acting on behalf of Grimmett, and that Kane was advised by Brocking that it would be legal to trade shares of ASO.

It is undisputed that outside of the one filing in 1952 under Regulation A and a later filing where the exemption sought under Regulation A was suspended, no effort was made to register ASO shares with the Commission. The massive distribution from the Mid-State holdings controlled by Grimmett was an obvious violation of the registration provisions of the Securities Act. Certain transactions, pursuant to Section 4 of the Securities Act, are exempted from the registration provisions of Section 5. It has long been the rule that the terms of an exemption from the Act are strictly construed against the claimant of its benefit[16/] and the claimant of an exemption has the burden of proof

16/ Securities and Exchange Commission v. Joiner Leasing Corp., 320 U.S. 344, 353, 355 (1943); Securities and Exchange Commission v. Sunbeam Gold Mines Co., 95 F. 2d 699 (C.A. 9, 1938); Cf. Black v. Magnolia Liquor Co., 355 U.S. 24, 26 (1957).

that the exemption is in fact applicable in his particular case.[17/] The above respondents have not pointed to any specific provision of Section 4 on which they rely. The two subsections that might apply are:

> "(1) transactions by any person other than an issuer, underwriter or dealer.
>
> (4) brokers' transactions executed upon customers' orders on any exchange or in the over-the-counter market but not the solicitation of such orders."

Subsection (4) cannot be relied on here by the respondents because the evidence clearly establishes that orders for ASO stock were actively solicited by salesmen of the registrant.[18/]

Subsection (1) also cannot be relied on because the term "underwriter" is defined in the Securities Act as follows:

> "(11) The term "underwriter" means any person who has purchased from an issuer with a view to, or offers or sells for an issuer in connection with, the distribution of any security, or participates or has a direct or indirect participation in any such undertaking . . . . .. As used in this paragraph the term "issuer" shall include, in addition to an issuer, any person directly or indirectly controlling or controlled by the issuer, or any person under direct or indirect common control with the issuer." (Section 2(11).

Grimmett, a person in control of ASO, was an issuer within the meaning of the above definition. Mid-State was under his control

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17/ Securities and Exchange Commission v. Ralston Purina Co., 346 U.S. 119 (1953).

18/ There is no dispute over the fact that the facilities of interstate commerce and of the mails were used by the registrant in its ASO transactions.

also and his alter ego. Registrant when it took shares emanating from Mid-State was participating in the distribution of such securities. Therefore, any exemption by virtue of the provisions of Section 4(1) is not available to registrant and has not been established.[19/] The argument of the above respondents in substance is that any violations which may have occurred were not willfully nor knowingly made.

One factor which stands out in Kane's version of his participation in the registrant's transactions in ASO stock is that he made no effort to check the information given him on ASO. He accepted Brocking's recommendation that registrant could trade in ASO even though he discharged Brocking for another reason. He knew that the ASO

19/ H. Carroll & Co., 39 S.E.C. 780 (1960); Associated Investors Securities, Inc., 41 S.E.C. 160 (1962).

The Commission has stated:

> "In summary, Section 4(1) is intended to exempt trading transaction [sic] with respect to securities already issued to the public, and it does not exempt distributions by issuers or control persons or the acts of other persons who engage in steps necessary to such distributions. 23/ (Sutro Bros. & Co., 41 S.E.C. 470, 477 (1963)).

23/ Cf. S.E.C. v. Chinese Consolidated Benevolent Association, 120 F. 2d 738 (C.A. 2, 1941), cert. denied, 314 U.S. 618; S.E.C. v. Culpepper, 270 F. 2d 241 (C.A. 2, 1959); S.E.C. v. Guild Films Company, Inc., 279 F. 2d 485 (C.A. 2, 1960)."

certificates purchased by registrant from Honnold all came from Mid-State; yet, he made no inquiry concerning this source of stock. His next biggest source of stock was Blair & Co. which was selling stock ostensibly for Gulihur. Here again, Kane made no inquiry.

On March 21, 1961 Grimmett sent Kane a Western Union money order for $2,000. Although Kane claimed that he has no recollection as to this payment, the money order bears an endorsement reading "David Paul Kane". (Div. Ex. 144, 144-A). On June 22, 1961 Grimmett drew a check on the PVNB to the order of Kane and Tallen in the amount of $4,200, which check bears the statement "Final settlement - Sale Certificate [No.] J-8509 ASO." While Kane's testimony is that he did not beneficially receive any of these funds, there is no evidence that he used the second payment as a basis for finding out from Tallen just what her stock dealings were with Grimmett and how such transactions might affect the interest of the registrant.

Kane had met Grimmett when the latter had made arrangements to purchase Fair Lady. He knew that two agreements with Grimmett had been unsuccessful and that Grimmett had given a check which was not good, had made no other payments and had borrowed substantial sums from Tallen. He also knew Grimmett's connection with ASO. He knew that Grimmett saw Tallen on occasion in Los Angeles and he made no effort to speak with Grimmett or to obtain further information on the source of supply of stock of ASO as well as its financial condition. The record establishes that Kane made no effort to obtain first-hand, reliable information on ASO but, instead, accepted unchecked information from secondary sources and kept aloof from supervising

trading transactions in that stock by his salesmen. The Commission has in many decisions dealt with the responsibility of a broker to avoid participation in the distribution to the public of substantial blocks of unregistered securities. The Commission summarized applicable law in the following language in a special release:

"Recent decision of the Courts and of the Securities and Exchange Commission have raised important questions concerning the standards of conduct expected of a registered broker-dealer in connection with the distribution to the public of substantial blocks of unregistered securities, particularly in situations where the securities are those of relatively obscure and unseasoned companies and where all of the circumstances surrounding the proposed distribution are not known to the broker-dealer. 1/

* * * * * *

"With regard to the registration requirements of the Securities Act of 1933, certain basic principles should be borne in mind. In the first place, Section 5 of the Securities Act of 1933 broadly prohibits the use of the mails or facilities of interstate commerce to sell a security unless a registration statement is in effect. A dealer or other person claiming the benefit of an exemption from this requirement has the burden of proving entitlement to it. 2/ Where unregistered securities are offered to a dealer for distribution, exemption is commonly claimed under the first and third clauses of Section 4(1) of the Securities Act which, speaking generally, exempt transactions not involving any distribution by, or for an issuer or for a person controlling, controlled by, or under common control with the issuer. Consequently,

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"1/ United States v. Francis Peter Crosby, 294 F 2d 928 (C.A. 2, 1961); SEC v. Culpepper, 270 F.2d 241 (C.A. 2, 1959); Gilligan, Will & Co. v. SEC, 267 F.2d 461 (C.A. 2, 1959); SEC v. Mono-Kearsarge, et al., 167 F. Supp. 248 (D. Utah, 1958); Barnett & Co., Securities Exchange Act Release No. 6310; Best Securities, Securities Exchange Act Release No. 6282.

"2/ SEC v. Ralston Purina, 346 U.S. 119 (1953); Gilligan, Will & Co. v. SEC, supra Note 1; SEC v. Culpepper, supra Note 1; and Edwards v. United States, 312 U.S. 473 (1941).

in order for this exemption to be available, a dealer must not be participating directly or indirectly in any such distribution. He may become such a participant even if he has no direct contractual relationship or privity with an issuer or person in a control relationship if he, in fact, engaged in steps necessary to such a distribution. 3/ Section 4(1) exempts trading transactions between individual investors with respect to securities already issued. It does not exempt distributions by issuers or control persons or acts of other individuals who engage in steps necessary to such distributions. 4/ Consequently, a dealer who offers to sell, or is asked to sell a substantial amount of securities must take whatever steps are necessary to be sure that this is a transaction not involving an issuer, person in a control relationship with an issuer or an underwriter. For this purpose, it is not sufficient for him merely to accept 'self-serving statements of his sellers and their counsel without reasonably exploring the possibility of contrary facts'. 5/

"The amount of inquiry called for necessarily varies with the circumstances of particular cases. A dealer who is offered a modest amount of a widely traded security by a responsible customer, whose lack of relationship to the issuer is well known to him, may ordinarily proceed with considerable confidence. On the other hand, when a dealer is offered a substantial block of a little-known security, either by persons who appear reluctant to disclose exactly where the securities came from, or where the surrounding circumstances raise a question as to whether or not the ostensible sellers may be merely intermediaries for, controlling persons or statutory underwriters, then searching inquiry is called for.

"3/ SEC v. Culpepper, supra Note 1.

"4/ SEC v. Chinese Consolidated Benevolent Association, 120 F. 2d 738 (1941), cert. denied, 314 U.S. 618; SEC v. Culpepper, supra Note 1.

"5/ SEC v. Culpepper, supra Note 1. See also SEC v. Mono-Kearsarge Consolidated Mining Company, supra Note 1.

> "The problem becomes particularly acute where substantial amounts of a previously little known security appear in the trading markets within a fairly short period of time and without the benefit of registration under the Securities Act of 1933. In such situations, it must be assumed that these securities emanate from the issuer or from persons controlling the issuer, unless some other source is known and the fact that the certificates may be registered in the names of various individuals could merely indicate that those responsible for the distribution are attempting to cover their tracks." (Securities Act Release No. 4445, February 2, 1962) 20/:

The fact that registrant only took a small portion of the block that was being distributed by Mid-State is no defense. As stated in Lewisohn Copper Corp., a distribution of securities comprises "the entire process by which in the course of a public offering the block of securities is dispersed and ultimately comes to rest in the hands of the investing public." 21/ The registrant by its activities played an important part in the distribution carried on by Grimmett and constituted a west coast outlet for ASO stock. The undersigned concludes that by their activities the registrant and Kane, a person in control of registrant, violated the registration provisions of the Securities Act and that such violations by the registrant and Kane were willful. 22/

20/ While this release was issued after the transactions in question here it does not set out new rules but summarizes existing law and quotes decisions antedating the activities involved in this proceeding.

21/ 38 S.E.C. 226, 234 (1958).

22/ See cases cited in footnote 14, supra.

The contention that respondents' conduct was protected because other brokers were dealing in ASO stock is without merit. There can be no general clearance for all shares of a security from registration requirements. An exemption, if any is available, attaches to transactions, not to an entire security.[23/] Whether specific shares have been properly registered or are exempt from registration depends on the particular circumstances. A broker cannot disregard his duty of making a careful inquiry when there are circumstances which reasonably should alert him that there may be a question of compliance with registration requirements. There were such circumstances here and the respondents in failing to take necessary steps to insure that their activities were not violative of the Securities Act failed to comply with applicable provisions.[24/]

C. Violations of Anti-Fraud Provisions of the Exchange Act By Certain Trading Activity By the Respondents While Interested In a Distribution of ASO Stock

Rule 10b-6 under the Exchange Act provides, in pertinent part, that:

23/ Gearhart & Otis, Inc., Sec. Exch. Act Rel. No. 7329 (June 2, 1964); Whitney & Company, 41 S.E.C. 699 (1963).

24/ Securities and Exchange Commission v. Mono-Kearsarge Consolidated Mining Co., supra, at p. 259; Atlantic Equities Co., Securities Exchange Act Rel. No. 7368 (July 14, 1964).

a) It shall constitute "a manipulative or deceptive device or contrivance" as used in Section 10(b) of the Act for any person,

1) who is an underwriter or prospective underwriter in a distribution of securities, or

2) who is the issuer or other person on whose behalf such a distribution is being made, or

3) who is a broker, dealer, or other person who has agreed to participate or is participating in such a distribution, directly or indirectly . . . either alone or with one or more other persons, to bid for or purchase for any account in which he has a beneficial interest, any security which is the subject of such distribution . . . or to attempt to induce any person to purchase any such security . . . until after he has completed his participation in such distribution.

It is alleged in the order for these proceedings that the registrant, Kane, and Tallen while engaged in the offer and sale of unregistered ASO stock violated the above provisions.

It has been found that Grimmett was engaged in a distribution of a substantial amount of ASO stock and that the respondents participated

therein. While engaged in this activity, the registrant also was engaged in open market activities in which Kane and Tallen bid for and purchased ASO stock on its behalf. These securities were placed in the account of the firm from which they were resold to customers on a dealer-principal basis.

It is contended on behalf of the registrant and Kane that registrant was not an underwriter as defined in Rule 10b-6c(1) (a person who has agreed with an issuer or other person on whose behalf a distribution is to be made to take part in the distribution). Relying on Bruns, Nordeman & Company, 40 S.E.C. 652 where the Commission said, ". . . a distribution is to be distinguished from ordinary trading transactions and other normal conduct of a securities business upon the basis of the magnitude of the offering and particularly upon the basis of the selling efforts and selling methods utilized." (p. 660); it is urged that registrant only was engaged in ordinary trading transactions since it sold at most 17,900 ASO shares or under 3% of the total distributed by Mid-State; neither registrant nor Kane published any written material concerning ASO; and Kane personally did not offer to sell or sell any ASO shares.

This argument ignores the following language used by the Commission just preceding that quoted, "The term 'distribution' as used in Rule 10b-6 is to be interpreted in the light of the rule's purposes as covering offerings of such a nature or magnitude as to require restrictions upon open market purchases by participants in order to prevent manipulative practices". (supra, p. 660) A broker may by his own efforts engage in selling activities of such magnitude as to constitute a distribution within the meaning of Rule 10b-6,[25/] but it is not necessary to find that each participant in a distribution shared in the distribution to such a degree.[26/] The entire course of the distribution must be evaluated, not just that of each individual broker. Here, there was a very substantial distribution of ASO stock stemming from Grimmett and registrant and Kane participated in it as set forth above. Finally, registrant's substantial sales of ASO stock within the time span of a few months might well be considered a major selling effort amounting to a distribution within the meaning of Section 10b-6, but the undersigned finds it unnecessary to rule on this question in view of the other findings made.

It is urged on Tallen's behalf that she did not "knowingly" participate in any violation of Rule 10b-6 because she did not know

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25/ Bruns, Nordeman & Company, supra; J. H. Goddard & Co., Inc., Sec. Exch. Act Rel. No. 7618 (June 4, 1965).

26/ Pennaluna & Company, Sec. Exch. Act Rel. No. 8063, p. 12 (April 27, 1967).

that registrant was acquiring ASO shares emanating from Grimmett. Tallen, as a trader for registrant and an officer had ample opportunity to observe the course of registrant's trading and learn from whom stock was being acquired. More than any salesman associated with Grimmett she had evidence from Grimmett that he was exercising an important influence on the trading in ASO stock.

It is concluded that the respondents willfully violated and willfully aided and abetted violations of Section 10(b) of the Exchange Act and Rule 17 CFR 240.10b-6 thereunder.

D. Fraud in the Sales of ASO Stock

1. Activities of Registered Representatives.

Investors who bought ASO stock from the registrant testified that highly optimistic statements were made to them by Tallen and other representatives -- Prince, Fleg, Winters and Fugita concerning ASO's assets, operations, and its stock. Witnesses testified that Tallen told them that there would be substantial price appreciation in ASO stock in a short time and that the stock would go up to $19 a share for sure; that it would go up from 15 to 50 points within six months; that it would go to 25 or 30 within a very short time; that if it were not purchased when it was selling at $3.50 a share it could not be purchased later at $10; the price would go up within six months; and that it would go to $10 within the next six months (the price range of the stock at the time Tallen allegedly made these representations was between $3 and $6.25 a share).

Tallen, who sold the most ASO stock of all registrant's representatives also, according to investor witnesses, spoke to them of ASO's financial condition, making such statements as: ASO was a producing company with very good income; that it was as good or better than AT&T; that it was a very good company with millions of dollars invested in Wilmington and Long Beach oil fields; that it was not a speculative security; that it was doing fabulously; that it was in good financial condition.

ASO had interests in Oklahoma and California. Some investors testified that they were told that ASO was doing very well in its operations. Some of the statements attributed to Tallen by investors were that ASO had an income from $18,000 to $20,000 a month from its Oklahoma properties; that it had producing wells and had other wells that were brought in and that ASO's oil holdings were worth $70 a share.

With respect to California operations, investors testified they were told by Tallen that ASO had won its case in a dispute over off-shore oil fields in the Wilmington Field and now had clear title to the property; that ASO owned three operating wells in the Long Beach area; that it had millions of dollars invested in the Wilmington and Long Beach oil fields and that it would begin drilling in two weeks (this statement was made in February 1961); that the president of ASO had put up $100,000 to start drilling oil; that ASO had producing wells and other wells in Long Beach; that it was digging

a well in Long Beach and that the oil was about to come in; that ASO had very good holdings in the Long Beach Field. These statements were made prior to July 12, 1961.

Tallen testified that she told all her customers that the ASO stock was highly speculative, there was litigation of the leases in the Long Beach area, purchasing the stock was strictly a gamble, if oil were found in the Long Beach area the stock would appreciate, and good companies were making a market in the stock. The testimony of eight investor witnesses establishes that Tallen told them a good deal more. The testimony of these witnesses, who came from diverse backgrounds and had no business or social connection with each other, was mutually corroborative and contained convincing detail. Their testimony is credited and it is found that Tallen made the statements set forth above. Witnesses also testified as to their transactions with other representatives -- Fleg, Prince, Fugita and Winters.[27/] Representations made to these investors by these representatives were very similar to those made by Tallen. Statements were made as to the extent of ASO's interest in Long Beach oil property, ASO's business in Oklahoma, the drilling program of ASO and the safety of an investment in ASO. These statements were also accompanied by optimistic predictions of sharp increases to be expected in the price of ASO stock within

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27/ Fugita and Winters were not specifically named in the order for proceedings. However, as employees, the registrant is responsible for their activities in the course of their regular duties.

a year or earlier. Where there were no outright representations as to ASO's income or losses or its property in Oklahoma there was a complete omission of any detail on these important factors. This was true in some instances in Tallen's dealings with customers also. This investor testimony is credited.

All of the above statements had no reasonable basis in fact. ASO had a record of completely unsuccessful operations from the time of its incorporation in 1952. During the period here pertinent, from 1960 to 1962, its financial condition showed increasing losses and earned surplus deficits. Losses were $15,588 in 1960, $19,016 in 1961 and $116,997 in 1962. Earned surplus deficits were $1,071,164 in 1960, $1,090,180 in 1961, and $1,207,000 in 1962. At no time in the period from October 1960 to August 1961 did its bank balance exceed $1,200.

ASO's record of operations in Oklahoma is one of failure. In 1952 ASO acquired leases to approximately 2,550 acres of water flood property in Nowata County, Oklahoma. The State of Oklahoma filed liens against this property in 1955 which Grimmett satisfied in 1957. He then purchased new leases for these properties which were later assigned to ASO. This property was never reworked nor redrilled and the development of two water flood projects in the area was never commenced. Part of the property was acquired by the U. S. Army Corps of Engineers in 1961 and 1962 in condemnation proceedings. The highest value placed on any part of the property

involved was $70 an acre on 50 acres. As this area had long been depleted of primary oil for production on a commercial basis the evaluation was based on values attributed to secondary oil recovery by way of water flood projects. At no time during the period that the Nowata County leases were owned by Grimmett or ASO or Mid-State, as nominee,were there any producing oil wells on nor was any income derived from this property.

ASO did not have any ownership interest in California oil properties until July 19, 1961. It never acquired any lease in the Wilmington Field located off shore of Long Beach. On June 30, 1961 Grimmett spoke with a W. S. Payne, Jr., a petroleum engineer, and learned from him that there was a lease called the Armstrong lease which needed financing. Arrangements were made for this lease to be assigned to ASO on July 11, 1961. This lease was ASO's first in California. Drilling of a well on this lease commenced July 12, 1961 and was completed six days later.

This well was not a success and Payne told Grimmett in August that while there was some production the well would never pay for its drilling and production costs. This well was located on a piece of land adjacent to the Long Beach city dump. On August 22, 1961 ASO obtained an assignment of two wells called the Dunlap No. 11 and No. 12. The Dunlap No. 11 well was redrilled and produced some oil. There was no further drilling made on behalf of ASO. Eventually, Payne offered $55,000 for the three leases to Grimmett and they were assigned to him on May 8, 1962. As a result of the operations

of the three wells ASO and Grimmett received a total of $14,162 in operating income for which $130,000 was advanced and a net deficit or loss was incurred of $60,838 on these wells.

In stockholders' reports and letters issued as of May 2, 1960, June 20, August 21 and August 31, 1961 (Div. Exs. 79-H and 74- H-J) ASO claimed ownership of a Dynamics Industries' lease purporting to give it rights in off shore areas in the Wilmington Field. The genesis of this claim is as follows: In 1956 Dynamics Industries filed a Complaint for Declaratory Relief based on its claim that it had a valid and binding contract with the City of Long Beach for possession of certain tidelands and submerged lands in the harbor of Long Beach for drilling oil and gas wells. In 1957 judgment was entered dismissing the action and granting judgment for the City. The judgment became final after appeal on June 4, 1959. Dynamics never was successful in its claim and never had a lease contract with the City of Long Beach.

In December 1959 Grimmett entered into a contract to purchase all of the outstanding stock of Dynamics. The shares involved were placed in escrow. On March 15, 1960 a complaint was filed on behalf of the shareholders of Dynamics seeking to recover the escrow shares because Grimmett failed to perform his contractual obligations. A judgment was filed on June 15, 1961 granting the return to Dynamics shareholders of their stock and assessing costs against Grimmett. Appeals from this judgment were finally denied in September 1962. At no time, therefore, did Dynamics have any

property rights in the Long Beach harbor nor did Grimmett or ASO through him have any rights to the Dynamics stock or any properties controlled by Dynamics. Therefore, any representations prior to July 1961 that ASO was drilling for oil in the Long Beach area were false, as were any representations at any time that ASO was drilling or about to drill in the Wilmington Field or any California off shore area.

Some investors also were told by Tallen and other representatives that ASO stock would be listed on the New York Stock Exchange or another national securities exchange, that it was going to merge with a well-known company. Standard Oil Company of California, Union Oil Company of California and Richmond Oil Company were mentioned in this connection. All of these statements had no basis in fact.

It has been established that registrant's representatives made predictions of sharp and quick price rises in the price of ASO stock, its possible listing on an exchange, and pending merger with a large established company, and misrepresented ASO's operations, assets, and its financial condition. At the same time there were omissions of significant details concerning ASO's financial condition, properties, earnings, and operations without which an investor could not approximate a reasonable evaluation of the value of an investment in ASO stock. The Commission has repeatedly held that a broker-dealer and his representatives must have a reasonable basis for representations

to customers of material facts about a security.[28] Known or reasonably available information necessary to provide the investor with a fair picture of a security must be disclosed.[29] The Commission has held that a prediction of a material rise in price of a speculative and promotional security of an unseasoned company within a short period of time is inherently fraudulent whether expressed in terms of opinion or fact.[30] ASO did not have basic qualifications for listing on the New York Stock Exchange and no evidence was presented that any action had ever been undertaken by ASO to secure listing on the New York Stock Exchange. False statements on this subject are violative of the anti-fraud provisions of the Securities Acts.[31]

28/ Mac Robbins & Co., Inc., Securities Exchange Act Rel. No. 6846, p. 4 (July 11, 1962), aff'd sub nom., Berke v. Securities and Exchange Commission, 316 F. 2d 137 (C.A. 2, 1963); Burton Corporation, 39 S.E.C. p. 211 (1959).

29/ D. F. Bernheimer & Co., Inc., 41 S.E.C. 358 (1963).

30/ Alexander Reid & Co., Inc., 40 S.E.C. 986 (1962); B. Fennekohl & Co., Securities Exchange Act Rel. No. 6898 (September 18, 1962); Heft, Kahn & Infante, Inc., Securities Exchange Act Rel. No. 7020 (February 11, 1963); Crow, Brourman & Chatkin, Inc., Securities Exchange Act Rel. No. 7839 (March 15, 1966); Hamilton Waters & Co., Securities Exchange Act Rel. No. 7725, p. 4 (Oct. 18, 1965).

31/ Aircraft Dynamics International Corp. Securities Exchange Act Rel. No. 7341 (June 11, 1964); Billings Associates, Inc., Securities Exchange Act Rel. No. 8217, p. 4-5 (December 28, 1967).

Similarly, misrepresentations as to pending mergers with well-known companies are fraudulent.[32/] The fact that a person deals in speculative securities and is told that a security is speculative does not excuse fraudulent representations made to him.[33/]

It is asserted on Tallen's behalf that any violations by her were not willful. Tallen maintained that she did all she could to obtain information on ASO and relied on information given her by people who presumably were reliable. She testified that Brocking, registrant's trader until the end of February 1961, told her that it was a good stock and that friends of his who were traders felt that way, that good houses were making a market in it and these firms would have researched the stock before they would have let their name appear in quotation sheets for the stock. Others she spoke to, according to her testimony, included a Dean Hart, a lawyer in Pauls Valley and a director of ASO who told her in February 1961 that the activity of ASO in Oklahoma and Long Beach was very promising, that Grimmett was an honorable man and that the litigation of the Long Beach property was being resolved. She also spoke with Larry Butler who was involved in the litigation, who told her that he felt the litigation could be successfully resolved and that Grimmett

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32/ Keith Richards Securities Corp., 39 S.E.C. 231 (1959); Huntington Securities Co., Inc., Securities Exchange Act Rel. No. 7842 (March 24, 1966); Underhill Securities Corporation, Securities Exchange Act Rel. No. 7668, p. 6 (August 3, 1965).

33/ R. Baruch & Co., supra, p. 7; Floyd Earl O'Gorman, Securities Exchange Act Rel. No. 7959, pp. 3, 4 (September 22, 1966); R. A. Holman & Co., Securities Exchange Act Rel. No. 7770, p. 9 (December 15, 1965).

owned the Dynamics lease. She also spoke with a Dr. Paul Torry in February 1961 who also assured her that Grimmett had the Dynamics lease and spoke of the Long Beach oil reserves. She also maintained that she spoke with Dudley Hughes of the Long Beach Harbor Department in February 1961 who told her that she could accept anything that Grimmett told her. She also received favorable reports on Grimmett from Arthur Cameron, an oil man from Oklahoma and Grimmett's brother, R. P. Grimmett.

Tallen admitted that she did not have any financial statement on ASO when she began selling ASO stock. The evidence establishes that no financial information was issued by ASO until June 1961 after most of the sales of ASO stock by registrant had been made. Tallen was in a position where she could have checked on some of the information furnished her by Grimmett and others. The litigation on the Dynamics lease was a matter of court record. It was a matter of record that the asserted lease of off shore oil land claimed by Dynamics had been held invalid. Any claims that drilling activity was underway in the Long Beach area on behalf of ASO prior to the drilling of the Armstrong well on July 12, 1961 could also have been easily checked on the scene. It also is surprising that Tallen, according to her version, accepted at face value high endorsements of Grimmett in view of the fact that he had reneged on two business deals with her and had borrowed substantial sums from her on which he was not making any repayment. None of the information furnished her warranted the extravagant statements made by Tallen. Under all the circumstances the undersigned concludes

that Tallen by misrepresentations about ASO and omissions to state material facts violated the anti-fraud provisions of the Securities Acts in her activities in the sale of ASO stock and that those violations were willful.[34/]

Tallen produced five investor witnesses in an effort to establish that she had not made misrepresentations in the sale of ASO stock. Apart from the fact that the testimony of some investor witnesses would not negate the fact that representations were made to others, the testimony of these witnesses themselves indicates that Tallen gave them incomplete information on ASO and also made some misrepresentations. Thus, she told one customer that ASO was in good financial condition and told two investors that ASO was drilling at Long Beach when there were no drilling operations there. To none of these investors did she make a full presentation of ASO's actual financial and operating condition. It is also concluded that the

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34/ The violation was compounded by the unrestrained nature of the misrepresentations made.

> A broker-dealer in his dealings with customers impliedly represents that his opinions and predictions respecting a stock which he had undertaken to recommend are responsibly made on the basis of actual knowledge and careful consideration. Without such basis the opinions and predictions are fraudulent, and where as here they are highly optimistic, enthusiastic and unrestrained, their deceptive quality is intensified since the investor is entitled to assume that there is a particularly strong foundation for them. And it is not a sufficient excuse that a dealer personally believes the representation for which he has no adequate basis. (Alexander Reid & Co., Inc., 40 S.E.C. 986, 990 (1962).

activities of other representatives for the registrant - Prince, Fleg, Fugita and Winters - in the sale of ASO were willfully violative of the anti-fraud sections of the Securities Acts.

2. Activities of the Registrant and Kane

Kane asserted that he had not heard of ASO in any detail before January 1961 when Brocking spoke to him briefly about it. Kane had met Grimmett in the course of the Fair Lady negotiations in 1959, but denied that he knew of the latter's connection with ASO at that time.

Kane left on a European trip in mid-January 1961 and returned at the end of February. He found that contrary to instructions he had given not to position any stock, two thousand shares of ASO had been bought. He ascribed this move to Brocking, testifying that Brocking told him he had bought ASO stock for inventory because he thought it would be a good situation for Kennedy, Cabot, that he had made a study of ASO, knew the traders of firms who were listed in the quotation sheets for it, and that a listing of a firm in the quotation sheets meant it had researched the stock and was satisfied with the underlying merits of the security. Tallen also told Kane she had checked with other people on ASO. Kane stated he discharged Brocking for violating his instructions but still relied on his recommendation. He also relied on Paul Gelles, a customer of registrant whom he regarded as a sophisticated investor, and who said he had investigated ASO and said it was a good company.

Kane left it to Tallen to convey information on ASO to registrant's representatives. He asserted that Tallen told him of representatives who made flamboyant statements and that he discharged them.

Kane was out of the country from July 7 to July 23 or 24, 1961, and denied any knowledge of Tallen's transactions with Gelles until after they occurred and stated he then criticized Gelles for his transactions with Tallen.

Kane further testified that he had had no discussions with Grimmett about ASO and made no effort to do so because he wanted to be "objective" about the stock. He denied knowing about any of his employees having acquired ASO shares from Grimmett or Mid-State, although he admitted that he knew Grimmett owed Tallen money and that she had received some ASO stock from him in cancellation of a debt due her. He further admitted that registrant had no current financial information on ASO during the period of registrant's major selling effort in ASO stock -- February thru May, 1961. Brocking and Tallen had also told him none were available.

It is urged on behalf of the registrant and Kane that Kane personally made no sales or offers to sell ASO stock, that Kane had no reasonable grounds to believe that representations made by the representatives of Kennedy, Cabot & Co., Inc. were not accurate in view of the information developed by Tallen, the investigations by others, and the shareholders' letters dated June 20,

August 21 and August 31, 1961, confirming information transmitted to Tallen and subsequently transmitted by her to Kane.

Although there is some evidence that Kane made some misstatements to investors and omitted important details in discussions[35/] there is no evidence of actual sales of ASO stock by Kane. However, this factor did not absolve him of responsibility. As the person in control of the operations of the registrant, it was his prime duty to supervise its sales representatives to see to it that customers were dealt with fairly and that fraudulent misstatements and omissions of material facts were not made by the representatives in sales presentations to investors. Representatives should not be left free of supervision[36/] and inexperienced personnel must be supervised carefully.[37/]

Kane admittedly relied on Tallen as the registrant's main source of information on ASO. He knew she was inexperienced in the securities field. He also knew she had had business dealings with

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35/ For example, Cyra Slater, testified that in November 1961 Kane told her an oil well had come in and suggested that she average down by purchasing more ASO stock. Edward T. Lynch testified he was told by Kane in June 1961 that ASO had a good chance to double in six months, was involved with leases in the Long Beach area, and was a good deal to buy. Their testimony is credited.

36/ L. B. Securities Corporation, Securities Exchange Act Rel. No. 7806, p. 4 (January 28, 1966).

37/ Schweikert & Co., Securities Exchange Act Rel. No. 7623, p. 4 (June 8, 1965); Sutro Bros. & Co., Securities Exchange Act Rel. No. 7052, p. 19-20 (April 10, 1963); Reynolds & Co., 39 S.E.C. 900, 917 (1960).

Grimmett which might have affected her objectivity as an adviser to investors. He, himself, had participated in business dealings with Grimmett which should have alerted him not to accept statements emanating from Grimmett at face value. No current financial statement on ASO was available during most of the period when registrant's sales were made. Yet the evidence indicates that Kane practically abdicated his functions of controlling the presentations made by his representatives to potential investors in ASO stock and left matters completely in the hands of Tallen.

Contrary to the claim of registrant and Kane that the representatives were carefully supervised, the evidence establishes that Tallen herself made extravagant statements about ASO which had no basis in fact. Prince, who participated in the violations, was retained in registrant's employ during the entire time ASO stock was sold by the registrant. In view of the extent of the fraudulent representations made by the representatives and the similarity of their representations indicative of a standard sales "pitch" and in view of the small size of the registrant's offices, it is inconceivable that Kane did not hear them; it is also concluded that any supervision he exercised was inadequate. 38/

38/ M. J. Merritt & Co., Inc., Securities Exchange Act Rel. No. 7878, p. 6 (May 2, 1966); Best Securities, Inc., 39 S.E.C. 931, 934 (1960); Leonard Lazaroff, Securities Exchange Act Rel. No. 7940, p. 4 (August 22, 1966).

The respondents contend that Kane had reasonable grounds to believe that the representations made by registrant's representatives were accurate and rely on Edgerton, Wykoff & Company, 36 S.E.C. 582 (1955). That case differs markedly from the instant case. In Edgerton a broker disseminated false information received from management. However, the Commission found that the broker had questioned certain data given him and received confirmatory information which reassured him and on which he relied. Here, no effort was made to check directly on information obtained from ASO. Secondary sources at most furnished generalities and not specific verification. Moreover, the representations made went beyond any information from management, i.e. exaggerated claims of quick, substantial stock price increases.

It is concluded that registrant and Kane by their aforementioned activities wilfully violated and aided and abetted violations of the anti-fraud provisions of the Securities Acts.

E. Excessive Mark-ups

The obligation of a broker-dealer to deal fairly with his customers includes the responsibility to sell securities to a customer at prices having a reasonable relationship to the prevailing market prices of the securities.[39/] Breach of the implied representation

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39/ Duker & Duker, 6 S.E.C. 384 (1939); Charles Hughes & Co., Inc. v. Securities and Exchange Commission, 139 F. 2d 434, 435-36 (2d Cir., 1943), cert. den. 321 U.S. 786 (1944).

that prices charged customers are reasonably related to the current market price without full disclosure to customers constitutes a fraudulent practice.[40/]

Absent countervailing evidence a dealer's contemporaneous cost is the best evidence of market price for the purpose of computing mark-ups.[41/]

From January 13 to August 8, 1961 registrant effected 107 transactions in ASO stock with its customers (Div. Ex. 55). In 34 of these transactions, mark-ups based on contemporaneous cost and range of dollar increments over contemporaneous cost were:

Number of Transactions	Percent Range	Dollar Range
4	8.3% - 9.1%	$12.50 - $100.00
25	13.6% -19.0%	$11.25 - $187.50
5	23.5% -95.7%	$22.00 - $850.00

"Contemporaneous cost" for this purpose is the price at which the dealer has bought such shares on the day of the sale to the customer, the preceding day, or the day after the sale.[42/]

40/ Associated Securities Corporation, 293 F. 2d 738 (10th Cir., 1961); Loss, Securities Regulation, 2nd ed., v. 3, pp. 1482-1487.

41/ Century Securities Company, Securities Exchange Act Rel. No. 8123, p. 7 (July 14, 1967); Langley-Howard, Inc., Securities Exchange Act Rel. No. 8361, p. 9 (July 25, 1968); Shearson, Hammill & Co., Securities Exchange Act Rel. No. 7743, p. 24, n. 57 (Nov. 12, 1965). Such a measure ". . . . merely reflects a recognition of the fact that the prices paid for a security by a dealer in actual transactions closely related in time to his sales are normally a highly reliable indication of the prevailing market price." Naftalin & Co., Inc., Securities Exchange Act Rel. No. 7220, p. 4 (Jan. 10, 1964).

42/ Securities and Exchange Commission v. Seaboard Securities Corp., C.C.H. Fed. Sec. Rep. § 91,697 ('64-'66 Dec.).

In the absence of definitive evidence of contemporaneous cost, another standard used is quotations in the National Daily Quotation Sheets. A broker-dealer's mark-up is computed by comparing the price charged the customer with the highest independent offer published in the sheets on the day of the sales transaction with the customer.[43/]

The figure arrived at by either of the foregoing methods is accepted as indicative of the prevailing market price in the absence of evidence to the contrary.[44/]

Of the 107 transactions registrant effected in ASO stock with its customers, 21 of such transactions had mark-ups over the highest offer published in the quotation or "pink" sheets as follows:

Number of Transactions	Percent Range	Dollar Range
7	6.5% - 8.7%	$ 2.50 - $106.88
10	10.7% -16.7%	$ 3.75 - $356.25
4	25%	$22.50 - $ 75.00

During the period from May 11 to June 9, 1961, Blair & Co. published a uniform ask price in the pink sheets of 5. This was substantially higher than all quotations by all the other brokers listed (Div. Ex. 13 and 14). During the period there were no transactions effected by Blair in the Gulihur account. If the Blair

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43/ Neftalin & Co., Inc., supra, pp. 5-6; Managed Investment Programs, 37 S.E.C. 783 (1937); Costello, Russotto & Co., Securities Exchange Act Rel. No. 7729, p. 3 (October 22, 1965).

44/ Charles Hughes & Co., Inc., supra, p. 438.

quotations are not considered as representative of the market because of the factors noted above,[45/] a revised computation of 39 transactions by registrant in ASO stock compared to the highest offer published in the pink sheets is as follows:

Number of Transactions	Percent Range	Dollar Range
12	6.5% - 8.7%	$2.50 - $125.00
18	10.7% - 20.0%	$3.75 - $356.25
9	23.5% - 33.3%	$22.50 - $300.00

It is asserted by respondents that no excessive mark-ups were charged to registrant's customers because respondents took care to obtain bona fide independent offers before engaging in transactions in ASO stock and ASO stock was sold by registrant reasonably near those prices.[46/]

Tallen testified that after Brocking left at the end of February 1961 there was no official trader for registrant. Tallen acted as trader using the pink sheet quotations and obtaining quotations over teletype. She determined the price to be charged customers with the aid on occasion of registrant's accountant. The general policy, she stated, was to charge about 3% above the market, but when she was asked the key question on how the charge was actually computed, she testified she could not recall the details. (Tr. p. ~~185~~ 1835)

Kane testified that the firm's accountant established guidelines with Brocking on pricing method. On principal transactions

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45/ C. A. Benson & Co., Inc., Securities Exchange Act Rel. No. 7856, p. 3 (Apr. 8, 1966).

46/ Loss, Securities Regulation, supra v. 3, p. 1491.

there was to be a charge of 2½ or 3%. However, when he was asked to what base the charge was added he stated that he would hesitate to state it ". . . because of the controversies and the charging of the pricing concepts and so on." (Tr. p. 2114). He further testified that Brocking told him that the average of the highest of the market quotations should be used as a basis for computing mark-up. No significance was placed by registrant on the price it paid for ASO stock in actual purchases, he added; the market price of the stock at the time of the particular transaction being used as a base.

The validity of the pink sheet quotations as a guideline was attacked by the respondents. Kane asserted that he obtained ASO quotations from time to time and that as a "fairly regular basis" telephone and teletype quotations varied from those in the pink sheets and were higher. Respondents produced 5 teletype slips that had higher offering prices on the particular days than the highest offer in the pink sheets. (Reg. Ex. 11A-E). However, in 4 instances the difference was 1/4th of a point and in another 1/8th. (Reg. Br. p. 11). Even disregarding the fact that quotations form the basis for negotiation and may be revised downward, these figures do not significantly affect computations previously made. Using these figures as a basis, mark-ups by registrant were generally above 10% and ranged to 25%. (Div. Reply Br. pp. 19-21).

The mark-ups charged by the registrant were beyond those considered reasonable under guidelines established in Commission

and court decisions.[47/]

Evidence presented by the respondents did not reveal with any definitiveness the actual procedures used by the respondents in fixing mark-ups and did not, in any event, outweigh the evidence presented by the Division of excessive mark-ups in a substantial number of sales of ASO stock. It is concluded that the respondents by their activities in fixing excessive mark-ups in the sale of ASO stock to customers, which practice was not revealed, willfully violated and aided and abetted violations of the anti-fraud provisions of the Securities Acts.

47/ J. A. Winston & Co., Inc., Securities Exchange Act Rel. No. 7337, p. 9 (June 8, 1964); Ross Securities, Inc., 40 S.E.C. 1064, 1066, fn. 5 (1964); Barnett v. U. S., 319 F. 2d 340 (C.A. 8, 1963).

III. CONCLUDING FINDINGS, PUBLIC INTEREST

The Commission, pursuant to the provisions of Section 15(b)(5) of the Exchange Act, so far as it is material herein, is required to censure, suspend for a period not exceeding twelve months or to revoke the registration of any broker or dealer if it finds that such action is in the public interest, and such broker or dealer, subsequent to becoming such, has willfully violated any provision of the Exchange Act, the Securities Act, or any rule or regulation thereunder. It also may, pursuant to the provisions of Section 15(b)(7) of the Exchange Act, censure, bar, or suspend for a period not exceeding twelve months any person from being associated with a broker or dealer if it finds that such sanction is in the public interest and that such person has willfully violated any provision of the Exchange Act, the Securities Act, or any rule or regulation thereunder.

It has been found that the respondents willfully violated and aided and abetted violations of the registration provisions of the Securities Act and the anti-fraud provisions of the Securities Acts.

The Division urges that in view of the key role played by Tallen in the registrant's activities involving ASO stock she should be permanently barred from association with any broker or dealer. It is argued in Tallen's behalf that she had been active as a registered representative for less than 60 days when she made her initial sales and investment in ASO stock; she received no supervision while

Kane was away from the office for a six-week period; that she relied on information supplied her by Grimmett and others; and that she disassociated herself from ASO and ceased selling its stock on receiving adverse information about it. It is further represented that since July 26, 1961, Tallen has limited her activities to being a finder and selling a small amount of mutual funds.

Ordinarily, conduct such as Tallen engaged in would warrant a permanent bar order. However, it is evident that the violations found stem from the activities of Grimmett as a root cause. Over a period of years he engaged in an elaborate scheme to defraud which involved illegal stock-selling practices backed by mis-representations of the operations and financial condition of ASO. Tallen, as a registered representative, should have been alert to danger signals and used avenues of inquiry to check on ASO and Grimmett, but failed in these responsibilities and sold ASO stock in substantial amounts. The undersigned concludes that in view of the inexperience of Tallen at the time of the violations and the complexities of the scheme concocted by Grimmett, a sanction short of a bar order, suspension for a period of one year, will adequately protect the public interest. Following the expiration of the suspension period she should not be associated with a broker-dealer except in a non-supervisory capacity, under such supervision as the Commission shall deem appropriate.

The Division has taken the position that in view of the violations committed by registrant and Kane it is in the public interest to suspend the registration of the registrant for a period not less

than 120 days and to suspend Kane for a period of not less than six months. On behalf of these respondents it is argued that Kane had no prior experience in the securities business before becoming president of registrant in May 1960; he was advised that it would be proper to trade ASO stock; sales of ASO stock by registrant were the result of activities by Tallen and Kane did not personally sell any of those shares; and Kane relied in good faith on representations from Tallen and others.

It is further pointed out that these respondents have not dealt in over-the-counter securities for more than six years; and that since February 1964, Kane has been president of an investment company, its investment advisor, and of the registrant, which acts as underwriter of the fund. Since that date neither Kane nor registrant has been otherwise engaged in the securities business. The factors set forth have all received consideration by the Commission as mitigating circumstances warranting less than maximum sanctions or no sanctions at all, respondents maintain.

The Commission has pointed out that, "the remedial action which is appropriate in the public interest depends upon the facts and circumstances of each particular case and cannot be precisely determined by comparison with action taken in other areas."[48/]

48/ Martin A. Fleishman, Securities Exchange Act Rel. No. 8002, p. 5 (Dec. 7, 1966); A. T. Brod & Company, Securities Exchange Act Rel. No. 8060, p. 6 (Apr. 26, 1967); Commonwealth Securities Corporation, Securities Exchange Act Rel. No. 8360, p. 8 (July 23, 1968).

The one circumstance which stands out in evaluating Kane's conduct is his inaction in the face of a substantial selling effort of ASO stock on the part of registrant's representatives. He had the prime responsibility for the proper conduct of registrant's operations, but remained relatively passive and did not maintain careful supervision over the ASO selling effort including the information available to representatives on ASO and the representations made to customers. The undersigned, giving due consideration to Kane's relative inexperience and other factors noted in the case of Tallen with reference to Grimmett, has determined that in view of the serious violations found, sanctions must be imposed on these respondents, but that maximum sanctions are not required. It is concluded that it is in the public interest to suspend the registration of the registrant for 120 days and to suspend Kane from association with a broker or dealer for a period of six months. 49/

Accordingly, IT IS ORDERED that Kennedy, Cabot & Co., Inc., be suspended from registration with the Commission for 120 days; that David Paul Kane be suspended from association with a broker-dealer for a period of six months; and that Linda D. Tallen be suspended from association with a broker-dealer for one year, and that following the expiration of the suspension period she shall not be

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49/ The Division has stated that it has no objection to registrant and Kane, during the period of a suspension order, entering into arrangements with other brokers and dealers to service customers of its All America Fund for which registrant is underwriter and Kane an officer. No such ruling can be made in advance of the submission of a concrete proposal.

associated with a broker-dealer except in a non-supervisory capacity, under such supervision as the Commission shall deem appropriate.

Pursuant to Rule 17(b) of the Commission's Rules of Practice a party may file a petition for Commission review of this initial decision within fifteen days after service thereof on him. This initial decision, pursuant to Rule 17(f) shall become the final decision of the Commission as to each party unless he files a petition for review pursuant to Rule 17(b) or 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 to review or the Commission takes action to review as to a party, this initial decision shall not become final as to that party. 50/

Sidney L. Feiler
Hearing Examiner

Washington, D. C.
August 27, 1968

50/ All contentions and proposed findings have been carefully considered. This initial decision incorporates those which have been found necessary for incorporation therein.