

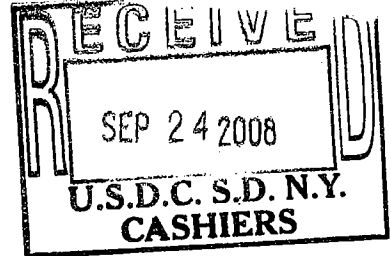
JUDGE SAND

09 CV 8265

**David Rosenfeld**  
**Associate Regional Director**

**Attorney for Plaintiff**  
**SECURITIES AND EXCHANGE COMMISSION**  
**New York Regional Office**  
**3 World Financial Center, Suite 400**  
**New York, New York 10281**  
**(212) 336-0153**

**UNITED STATES DISTRICT COURT**  
**SOUTHERN DISTRICT OF NEW YORK**



**SECURITIES AND EXCHANGE COMMISSION,**

**Plaintiff,**

**-against-**

**MELVYN NATHANSON, ERIC NATHANSON,**  
**CHARLES PETEREIN, and GANIS COMPANY, INC.,**

**Defendants.**

**Civil Action No.**

**COMPLAINT**

Plaintiff Securities and Exchange Commission ("Commission"), for its complaint against defendants Melvyn Nathanson ("M. Nathanson"), Eric Nathanson ("E. Nathanson"), Charles Peterlein ("Peterlein"), and Ganis Company, Inc. ("Ganis") (the "Defendants"), alleges as follows:

**SUMMARY OF ALLEGATIONS**

1. This action concerns securities fraud committed by three individuals and a corporate entity involved in the securities lending, or "stock loan," business. From July 2003 through April 2005, the Defendants defrauded two securities brokerage firms out of a total of at least \$1.16 million through the payment of sham finder fees and undisclosed kickbacks that ultimately came out of the pockets of the two brokerage firms.

2. Peterein was the stock loan trader in charge of the securities lending desk at PAX Clearing Corp. ("PAX"), a Chicago-based registered broker-dealer, and M. Nathanson and E. Nathanson operated a now-defunct stock loan finder firm based in Florida called SME Consultants, Inc. ("SME"). Through SME, M. Nathanson and his son E. Nathanson worked as consultants to Kellner, Dileo & Co. ("Kellner"), a registered broker-dealer based in New York City, and were paid to arrange stock loan transactions for Kellner. Pursuant to the Defendants' scheme, Peterein caused PAX to engage in stock loans with Kellner on terms that deliberately favored Kellner at PAX's expense and increased the amount of compensation that Kellner paid to SME. In exchange, M. Nathanson and E. Nathanson directed kickbacks to Peterein by causing Kellner to pay sham finder fees on those stock loan transactions to Ganis, a shell-company controlled by Peterein. The fees paid to Ganis were a sham because, unbeknownst to Kellner, Ganis did not perform any finding or other legitimate services on the transactions. In addition, Peterein never told PAX that Peterein was receiving payments from Kellner, much less that the payments were kickbacks arranged by M. Nathanson and E. Nathanson to compensate Peterein for directing stock loan transactions to Kellner at rates that purposely disadvantaged PAX in order to generate payments to both SME and Ganis.

3. Peterein, M. Nathanson and E. Nathanson caused PAX and Kellner to engage in over 4,000 stock loans pursuant to their scheme, with Kellner paying a total of approximately \$651,580 to SME and a total of approximately \$513,788 to Ganis in sham finder fees.

4. By virtue of the foregoing conduct, each of the Defendants, directly or indirectly, singly or in concert, violated Section 17(a) of the Securities Act of 1933 ("Securities Act") [15 U.S.C. § 77q(a)], Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5]; and each of them is also

liable in the alternative, pursuant to Section 20(e) of the Exchange Act [15 U.S.C. § 78t(e)], for aiding and abetting the violations of Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5] committed by those Defendants with whom they schemed. Unless each of the Defendants is permanently restrained and enjoined, they will again engage in the acts, practices, transactions and courses of business set forth in this complaint and in acts, practices, transactions and courses of business of similar type and object.

### **JURISDICTION AND VENUE**

5. The Commission brings this action pursuant to the authority conferred by Section 20(b) of the Securities Act [15 U.S.C. § 77t(b)] and Section 21(d) of the Exchange Act [15 U.S.C. § 78u(d)], and seeks to restrain and enjoin the Defendants permanently from engaging in the acts, practices, transactions and courses of business alleged herein. The Commission also seeks a final judgment ordering the Defendants to disgorge their ill-gotten gains and pay prejudgment interest thereon, and ordering the Defendants to pay civil money penalties pursuant to Section 20(d) of the Securities Act [15 U.S.C. § 77t(d)] and Section 21(d)(3) of the Exchange Act [15 U.S.C. § 78u(d)(3)].

6. This Court has jurisdiction over this action, and venue lies in this District, pursuant to Sections 20(d) and 22(a) of the Securities Act [15 U.S.C. §§ 77t(d) and 77v(a)] and Sections 21(d) and 27 of the Exchange Act [15 U.S.C. §§ 78u(d) and 78aa]. The Defendants, directly and indirectly, have made use of the means or instrumentalities of, or the means or instruments of transportation or communication in, interstate commerce, or of the mails, or of the facilities of a national securities exchange, in connection with the transactions, acts, practices and courses of business alleged herein. Some of these transactions, acts, practices and courses of business occurred in the Southern District of New York, where each of the Defendants transacted

business during the relevant period. For example, the stock loan transactions at issue here were entered into and recorded on Kellner's books at Kellner's principal place of business in New York, New York, and the finder fee payments that Kellner made to SME and Ganis originated from Kellner's principal place of business in New York, New York.

### **THE DEFENDANTS**

7. **M. Nathanson**, age 70, resides in Lady Lake, Florida. He currently operates a Florida corporation named MAG Consultants, Inc. ("MAG"), which has a consulting agreement with Newedge USA, LLC ("Newedge"), a registered broker-dealer with its principal place of business in New York, New York. From at least October 1998 to March 2006, M. Nathanson worked as a stock loan finder with SME, which he effectively controlled.

8. **E. Nathanson**, age 43, resides in Lady Lake, Florida. He is currently employed as a stock loan trader with Newedge. From October 1998 to March 2006, he worked as a stock loan finder with SME.

9. **Peterein**, age 59, resides in Evergreen Park, Illinois. He is currently employed as a stock loan trader with Sallerson-Troob, LLC, a registered broker-dealer with its principal place of business in Chicago, Illinois. From September 2000 to May 2005, Peterein was a principal associated with PAX, a registered broker-dealer, and ran PAX's stock loan trading desk.

10. **Ganis** is an Illinois corporation with a business address in Evergreen Park, Illinois. Peterein and his wife are both officers of Ganis, but Peterein alone effectively controls Ganis and its bank account.

## **RELEVANT ENTITIES**

11. **SME** is a Florida corporation that, during the relevant period, had a business address in Summerfield, Florida. SME filed for administrative dissolution in September 2007 and is now defunct. M. Nathanson effectively controlled SME and ran its overall business, and E. Nathanson was responsible for SME's day-to-day stock loan activities. During the relevant period, SME had a stock loan consulting arrangement with Kellner.

12. **PAX** was registered with the Commission as a broker-dealer during the relevant period and maintained its principal place of business in Chicago, Illinois. In March 2005, PAX was acquired by Merrill Lynch & Co., Inc. and now does business as the PAX Division of Merrill Lynch Professional Clearing Corp.

13. **Kellner** is registered with the Commission as a broker-dealer and an investment adviser. Kellner is now known as KDC Merger Arbitrage Fund, LP and maintains its principal place of business in New York, New York.

## **BACKGROUND**

### **Structure Of Stock Loan Transactions**

14. A securities loan is a collateralized, temporary exchange of securities. The collateral is usually cash or other securities. Under the terms of the standard loan agreements that govern these transactions and as a matter of industry practice, borrowers are free to re-lend, sell or otherwise do as they please with the stock, subject only to satisfying the obligation to return the same number of shares at the end of the loan term. Financial institutions borrow securities for different purposes. For example, a broker-dealer may need to borrow securities to cover short sales or a bank may wish to lend securities to gain short-term access to cash. If the security is liquid (*i.e.* readily available and thus called "easy-to-borrow"), the financial institution borrowing

the security receives interest for the duration of the loan on the cash collateral it makes available to the lender. The interest payment is called a “rebate.” If the security is in limited supply (*i.e.* “hard-to-borrow”), the borrower generally pays interest to the lender for the right to borrow the security. This interest payment is called a “negative rebate.” The rebates and negative rebates are a percentage of the total market value of the securities and are quoted as annual percentage rates. Stock loan transactions may stay open for as little as one trading day or as long as several months or even a year.

### **Role And Compensation Of Finders**

15. In the past, stock loan traders typically employed the services of finders to locate hard-to-borrow stock. In today’s securities market, however, traders rarely need the services of finders. Technological advances and other improvements have made it easier and faster for traders to locate hard-to-borrow securities on their own. On April 29, 2005, the New York Stock Exchange issued an advisory opinion cautioning all member firms about continuing to do business with finders and stating: “We have seen only limited instances where a finder is actually providing services that an effective stock loan department could not provide.”

16. The stock loan finder’s fee would typically be negotiated by the lender and borrower as part of the terms of the stock loan and, like the rebate rate, would be expressed as a percentage of the total market value of the stock.

17. The rebates and finder fees are calculated and paid on a daily basis, and the brokerage firms and finders continue to receive payments until the borrowed stock is returned or recalled. Accordingly, loans that remain open for extended periods generate substantial profits for both broker-dealers and finders.

## THE DEFENDANTS' FRAUDULENT SCHEME

### Overview And Structure Of The Scheme

18. From July 2003 through April 2005, M. Nathanson, E. Nathanson and Peterein engaged in a kickback scheme that defrauded PAX and Kellner out of approximately \$1.16 million in connection with over 4,000 stock loan transactions.

19. During the relevant period, M. Nathanson and E. Nathanson operated SME, a finder firm that had a consulting arrangement with Kellner since May 2002. Pursuant to an oral agreement, SME was authorized to solicit securities lending transactions on behalf of Kellner, with SME essentially acting as a stock loan finder for Kellner. SME was authorized to contact third parties directly on Kellner's behalf and solicit them to engage in stock loan transactions with Kellner. The terms of the transactions that SME arranged were communicated to Kellner's stock loan department and the loans were recorded on order tickets and in Kellner's stock loan trading records. Kellner paid SME 40% of the profit generated by each transaction arranged by SME.

20. In mid-2003, amid concerns that PAX was going to be acquired by another firm, Peterein and M. Nathanson, who had been friends since the 1970s, devised a fraudulent scheme to enable them both to profit illicitly from PAX's stock loan trading. M. Nathanson and Peterein agreed that: (a) Peterein would set up a shell company that would purport to be a finder firm; (b) Peterein would direct a large volume of PAX stock loan business to SME on terms that were favorable to Kellner and unfavorable to PAX; and (c) in exchange, M. Nathanson would direct kickbacks to Peterein disguised as finder fee payments to Peterein's shell company.

21. On July 22, 2003, Peterein formed and incorporated his shell-company, Ganis. In Ganis' corporate filings, Peterein listed his own home address as Ganis' business address and

named himself and his wife as the only corporate officers. M. Nathanson directed Peterein to send the relevant corporate information about Ganis to E. Nathanson. On July 28, 2003, Peterein sent an email from his home email account to E. Nathanson with the corporate information for Ganis. On July 29, 2008, E. Nathanson forwarded the information to Kellner in order to have Ganis listed as an "approved" stock loan finder firm on Kellner's books.

22. Ganis became authorized to receive finder fees from Kellner in connection with stock loans on which Ganis performed finding services that benefited Kellner. M. Nathanson and E. Nathanson knew that Ganis was Peterein's alter ego and that by arranging for Ganis to receive payments from Kellner in connection with PAX stock loan orders, M. Nathanson and E. Nathanson were in reality arranging for Peterein to receive payments from Kellner on those transactions. Neither M. Nathanson nor E. Nathanson ever told anyone at Kellner that Ganis was controlled by Peterein.

#### **Mechanics Of The Loans And Undisclosed Kickback Payments**

23. After Peterein's kickback arrangement with the Nathansons was in place, Peterein steadily increased the volume of stock loan transactions that PAX engaged in with Kellner via SME, thereby increasing the amount of both the payments that SME received and the kickback payments that Peterein received pursuant to the scheme. For example, in July 2003 -- the first month of the scheme -- Peterein arranged 43 stock loan transactions between PAX and Kellner. In November 2003, Peterein arranged 238 such transactions. In May 2004, the monthly total rose to 451 transactions, and by October 2004, the monthly total rose to 538 transactions.

24. Over the course of 17 months -- from July 2003 through November 2004 -- Peterein arranged a total of approximately 4,034 stock loan transactions between PAX and Kellner on which both SME and Ganis were paid "finder fees" pursuant to the Defendants'



scheme. In December 2004, Kellner stopped paying all finder firms other than SME, and Peterein stopped arranging for stock loan transactions between PAX and Kellner. Although Kellner stopped paying Ganis, SME continued to receive payments from Kellner through April 2005 on the PAX-Kellner stock loan transactions that were entered into prior to December 2004 and which remained open on Kellner's books.

25. Generally, each trading day, Peterein or another PAX employee acting at Peterein's direction spoke with either E. Nathanson or M. Nathanson about the securities that PAX had available to loan or wished to borrow and the interest rate at which PAX would enter into the transaction with Kellner. Either E. Nathanson or M. Nathanson, or someone acting on their instructions, then conveyed the terms of the loan to Kellner, either by calling in the loan information and a request for Ganis to be paid a finder fee or by faxing order tickets to Kellner that listed Ganis as a finder entitled to payment. In doing so, the Nathansons and SME falsely represented to Kellner that Ganis had worked on the transaction as a finder and was entitled to receive a finder fee. These representations were false because Ganis was not involved in arranging any of the stock loans for which Ganis was paid by Kellner, and Peterein was being paid by PAX as a trader to act in PAX's best interests. In making the payments to Ganis, Kellner relied on the false information provided by SME and the Nathansons and on the fact that Ganis had been placed on Kellner's approved finder list at the Nathansons' behest.

26. Pursuant to the Defendants' scheme, Peterein caused PAX to engage in stock loan transactions with Kellner at interest rates that were deliberately unfavorable to PAX, *i.e.* at rates that were inferior to the generally available market rates that other firms were willing to pay or receive for those stocks. Peterein did so to in order to guarantee Kellner a sufficient profit from which to pay both Ganis and SME when it re-loaned the stock to, or borrowed the stock from,

another firm. As the following transaction illustrates, the difference in interest rates enabled the Nathansons to cause Kellner to pay a sham finder fee to Ganis while still leaving room for Kellner and SME to make a profit as well.

27. On March 19, 2004, Peterein caused PAX to lend 15,600 shares of AMKOR TECH stock to Kellner at a positive rebate rate of 1.55% (*i.e.* PAX received the cash collateral but paid interest at that rate to Kellner because the stock was “easy to borrow”). That same day, either M. Nathanson or E. Nathanson arranged for Kellner to loan 15,600 shares of the same stock to another firm at a lower positive rebate rate of 1.15% (*i.e.* Kellner received the cash collateral but paid interest at that rate to the other firm). The difference between the higher rate that Kellner received from PAX and the lower rate that Kellner paid to the other firm was 0.40%, and the Nathansons allocated Kellner’s profit margin as follows: Ganis and SME each received payment equal to 0.15% of the shares’ market value -- or a total of 75% of the profit generated by the transaction -- leaving Kellner with the remaining 0.10%. This transaction remained open for 61 days and resulted in Kellner paying Ganis and SME a total of \$72.69 each.

28. PAX was defrauded in the above transaction because Peterein knowingly caused PAX to pay as much as 0.40% more than it would have paid in an arms-length transaction, and Peterein diverted funds equal to 0.15% to himself. Kellner was also defrauded because Kellner paid Ganis and SME a substantial portion of Kellner’s profit on the transaction even though, unbeknownst to Kellner: (i) Ganis did not perform any services and was simply acting as a conduit for a kickback payment to Peterein; and (ii) M. Nathanson and E. Nathanson arranged the transaction pursuant to their fraudulent scheme with Peterein for the purpose of generating a kickback payment to Peterein and higher fees for SME. Although Kellner was the firm that actually paid the fees, PAX was the ultimate victim of the fraud, as those fees were made

possible by the artificially large spread in the lending rates that Peterein created by causing PAX to pay a higher positive rebate rate to Kellner than PAX would have paid in an arms-length transaction. Accordingly, the fees paid to Ganis and SME effectively came out of PAX's pocket.

29. To ensure that Peterein received his kickback payment each month, E. Nathanson conveyed to Peterein's niece, who came to Peterein's home once a month to keep Ganis' books, the dollar amount of the monthly invoice that Ganis needed to send to Kellner. At Peterein's direction, Peterein's niece entered the dollar amount provided by E. Nathanson into a form invoice and then emailed or faxed the invoice to Kellner. Upon receiving Ganis's invoice each month, Kellner paid Ganis by wire transfer or check.

30. On at least one occasion, M. Nathanson paid Peterein a cash kickback. In February 2005, M. Nathanson personally handed Peterein \$10,000 in cash stuffed in an envelope as payment for the open stock loan transactions for which Ganis was no longer being paid by Kellner.

31. Kellner paid Ganis a total of approximately \$513,788 in sham finder fees during the course of the scheme, which Peterein then transferred to his personal bank accounts. Likewise, the Nathansons profited from their fraudulent arrangement with Peterein by collecting approximately \$651,580 from Kellner through SME on the same transactions. Peterein directed these transactions to SME because M. Nathanson and E. Nathanson agreed and arranged to pay kickbacks to Peterein through Ganis.

32. Peterein did not inform the compliance personnel or his partners at PAX that he was deliberately causing PAX to enter into stock loan transactions at rates that were unfavorable to PAX pursuant to an arrangement with M. Nathanson and E. Nathanson. Nor did Peterein disclose to anyone else at PAX that he owned and controlled a company that was being paid by another brokerage firm to compensate Peterein for causing PAX to engage in those transactions.

Neither M. Nathanson nor E. Nathanson, nor anyone else associated with SME, disclosed to anyone at Kellner anything about the true nature of the kickback arrangement that M. Nathanson and E. Nathanson had with Peterein and Ganis.

### **CLAIMS FOR RELIEF**

#### **Violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5**

33. The Commission realleges and incorporates by reference herein each and every allegation contained in paragraphs 1 through 32.

34. The Defendants directly or indirectly, singly or in concert, by use of the means or instruments of transportation or communication in, or the means or instrumentalities of, interstate commerce, or by the use of the mails, or of the facilities of a national securities exchange, in the offer or sale and in connection with the purchase or sale of securities, knowingly or recklessly, have: (a) employed devices, schemes and artifices to defraud; (b) obtained money or property by means of, or otherwise made, untrue statements of material fact, or have omitted to state material facts necessary in order to make statements made, in light of the circumstances under which they were made, not misleading; and/or (c) engaged in acts, transactions, practices and courses of business which operated or would have operated as a fraud or deceit upon purchasers of securities and upon other persons.

35. As part and in furtherance of the fraudulent scheme and other violative conduct described above, each of the Defendants, directly or indirectly, singly or in concert, employed the deceptive devices, schemes, artifices, contrivances, acts, transactions, practices and courses of business and/or made the misrepresentations and/or omitted to state the facts alleged above in paragraphs 1-3 and 18-32.

36. The false and misleading statements and omissions made by the Defendants, more fully described above in paragraphs 1-3 and 18-32, were material.

37. The Defendants knew, or were reckless in not knowing, that these material misrepresentations and omissions, more fully described above in paragraphs 1-3 and 18-32, were false or misleading, and the Defendants otherwise acted with the requisite scienter by knowingly or recklessly engaging in the fraudulent scheme described above in paragraphs 1-3 and 18-32.

38. By reason of the acts, statements, omissions, practices, and courses of business alleged herein, the Defendants, singly or in concert, directly or indirectly, have violated, and unless enjoined will again violate, Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)], Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

39. By reason of the foregoing and pursuant to Section 20(e) of the Exchange Act, each of the Defendants, singly or in concert, directly or indirectly, also aided and abetted each other's primary violations by knowingly providing substantial assistance to the other defendants' violations of, and unless enjoined will again aid and abet violations of, Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

#### **PRAYER FOR RELIEF**

**WHEREFORE**, the Commission respectfully requests that this Court enter a Final Judgment:

#### **I.**

Permanently enjoining and restraining each of the Defendants, their agents, servants, employees and attorneys and all persons in active concert or participation with them who receive actual notice of the injunction by personal service or otherwise, and each of them, from violating,

directly or indirectly, Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)], Section 10(b) of the Exchange Act [15 U.S.C. §§ 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

**II.**

Ordering each of the Defendants to disgorge the ill-gotten gains they received from the violations alleged herein, and to pay prejudgment interest thereon.

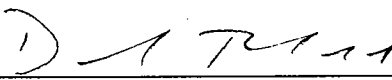
**III.**

Ordering each of the Defendants to pay civil monetary penalties pursuant to Section 20(d) of the Securities Act [15 U.S.C. § 77t(d)] and Section 21(d)(3) of the Exchange Act [15 U.S.C. § 78u(d)(3)].

**IV.**

Granting such other and further relief as the Court deems just and proper.

Dated: New York, New York  
September 24, 2008

  
\_\_\_\_\_  
David Rosenfeld  
Associate Regional Director

Attorney for Plaintiff  
SECURITIES AND EXCHANGE COMMISSION  
New York Regional Office  
3 World Financial Center, Suite 400  
New York, New York 10281  
(212) 336-0153

Of Counsel:

George N. Stepaniuk  
Joseph Dever  
Burk Burnett  
Kenneth V. Byrne  
Karen Lee