ADMINISTRATIVE PROCEEDING
FILE NO. 3-2869

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of	
NEWPORT SECURITIES CORP. (8-14255)	
A. GURDON WOLFSON	
MARTIN SUSSON	
ROY O. DAWSON	

FILED
FEB 16 1973
SECURITIES & EXCHANGE COMMISSION

INITIAL DECISION

February 16, 1973
Washington, D. C.

Ralph Hunter Tracy
Administrative Law Judge

ADMINISTRATIVE PROCEEDING
FILE NO. 3-2869

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of NEWPORT SECURITIES CORP. (8-14255) A. GURDON WOLFSON MARTIN SUSSON ROY O. DAWSON	INITIAL DECISION

APPEARANCES: Theodore A. Levine and William C. Turner for the Division of Enforcement

Thomas W. Armstrong and John A. Dudley of Sullivan and Worcester for Newport Securities Corp., A. Gurdon Wolfson, Martin Susson and Roy O. Dawson.

BEFORE: Ralph Hunter Tracy, Administrative Law Judge

THE PROCEEDINGS

These are public proceedings instituted by an order of the Commission ("Order") dated March 3, 1971, pursuant to Sections 15(b) and 15A of the Securities Exchange Act of 1934 ("Exchange Act") to determine whether the above named respondents, among others, [1] committed various charged violations of the Securities Act of 1933 ("Securities Act") and the Exchange Act and regulations thereunder as alleged by the Division of Enforcement ("Division") and the remedial action, if any, that might be appropriate in the public interest.

The proceeding has been determined as to four respondents as indicated, and this initial decision is, therefore, applicable only to the remaining respondents. However, it will necessarily, in view of the nature of the charges and of the factual circumstances, also, involve findings concerning some or all of those four respondents.

The order for proceedings alleges, in substance, that during the period from approximately January 1, 1969 to January 31, 1970, [2]

1/ The order also sets forth charges against the following persons whose cases have been determined by the Commission as reflected in the Commission's respective releases as noted: Glen Elwood Clymore, Stuart Warren Fine and Burdett Richard Harrison, Exchange Act Release No. 9409, dated December 7, 1971 and Rex Richard Reno, Exchange Act Release No. 9735, dated August 21, 1972.

2/ An amendment to the order which changed "January 1970" to "January 31, 1970" was allowed by the Administrative Law Judge during the course of the hearing. (TR. 2474)

Newport Securities Corp. ("Newport"), A. Gurdon Wolfson ("Wolfson"), Martin Susson ("Susson"), and Roy O. Dawson ("Dawson"), singly and in concert, willfully violated and willfully aided and abetted violations of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder in connection with effecting transactions in the common stock of Hydro Tech Corporation ("Hydro Tech"), Instrument Technology Corporation ("Instrument Tech"), Micro Tenna Corporation ("Micro Tenna"), Audio Visual International Corporation ("AVI), Development Corporation of America ("DCA"), Hill Brothers, Inc., ("Hill Bros."), Shell's City, Inc., ("Shell's City"), International Book Corp., ("IBC"), Aero Systems, Inc., ("Aero Systems"), Honeycomb Systems, Inc., ("Honeycomb"), American Foods, Inc., ("American Foods"), Imperial Industries, Inc., ("Imperial Industries") and Resort Car Rental Systems, Inc. ("Resort Car"), by means of untrue statements of material facts and omissions to state material facts necessary in order to make the statements made, in the light of the circumstances under which they were made not misleading. The order also alleges that from January 1, 1969 to September 1969 Newport, Wolfson, Susson and Dawson willfully violated and willfully aided and abetted violations of Section 10b of the Exchange Act and Rule 10b-6 thereunder in that while participating in a distribution of the common stock of DCA, Shell's City and Hill Bros. they bid for and purchased such securities for accounts in which they had a beneficial interest and induced others to purchase said securities prior to completing said distribution. The order alleges, further, that from on or about

January 1969 to January 1970, Newport willfully violated and Wolfson and Susson willfully aided and abetted violations of Section 7(c)(1) of the Exchange Act and the rules and regulations prescribed thereunder concerning the arranging, extending and maintaining of credit to and for customers on securities; and during the relevant periods indicated above, Newport, Wolfson, Susson and Dawson failed to reasonably supervise persons subject to their supervision with a view to preventing the violations alleged in the order.

The evidentiary hearing was held at Los Angeles, California, from October 7 to October 29, 1971, and from January 10 to January 20, 1972, with all respondents being represented by counsel. Proposed findings of fact and conclusions of law and supporting briefs were filed by the remaining parties to the proceedings.

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

FINDINGS OF FACT AND LAW

Respondents

Newport was organized by Wolfson, Dawson and Susson, who contributed equally to its capitalization, and was incorporated under the laws of the State of California on September 3, 1968. Newport was registered with the Commission pursuant to Section 15(b) of the Exchange Act on December 1, 1968 and is a member of the National Association of Securities Dealers ("NASD"). It maintains offices at 1617 Westcliff Drive, Newport Beach, California.

A. Gurdon Wolfson ("Wolfson"), president and a director of Newport has been a securities salesman since April 1966 having been with J. C. Roberts & Co. and Executive Securities Corp. Prior to April 1966 he was engaged in the real estate business.

Roy O. Dawson ("Dawson") vice-president, treasurer and a director of Newport has been in the securities business since June 1961. From June 1961 to July 1964 he was a registered representative with Eastman Dillon, Union Securities & Co., and from August 1964 to January 1965 he was a registered representative and from January 1965 to September 1968 was a vice president of Roberts, Scott & Co., Inc. Prior to June 1961 he was in the tire business.

Martin Susson, vice-president, secretary and a director of Newport was associated with United Benefit Life Insurance Company, as a salesman, for 22 years preceding his association with Newport.

Organization of Newport

Newport was incorporated under the laws of the state of California on September 3, 1968, to engage in business as a broker-dealer and to conduct a general investment banking business. The idea for the formation of Newport originated with Roy O. Dawson and Rex Reno ("Reno") during 1967 when both were employed at the brokerage firm of Roberts, Scott & Co., Inc., at its Laguna Beach, California, office.

During the 1968 Labor Day weekend Dawson had discussions with Susson and Wolfson concerning their participation in Newport. As a result of these discussions Susson, Dawson and Wolfson each

contributed equally to the capitalization of Newport and it filed a broker dealer registration with the SEC which became effective on December 1, 1968. On December 20, 1968, Newport became a member of the NASD and began operations on the same day.

It had been contemplated that Reno would become an equal partner but at the time Newport was capitalized and began business he was under a 60 day suspension ordered by the Commission.[3/] Accordingly, it was agreed that if and when he was free to do so he would join the firm. He became a registered representative at Newport in February 1969 continuing in that capacity until October 1969. In connection with the employment of Reno, Wolfson filed an affidavit with the California Commission of Corporations stating that Reno's activities would be subject to his supervision.

Violations of the Anti-Manipulative Provisions Under the Exchange Act

The order for proceedings alleges that from January 1, 1969 to September 1969, all of the respondents named in the order, willfully violated and willfully aided and abetted violations of section 10(b) of the Exchange Act and Rule 10b-6 thereunder while participating in distributions of the common stock of DCA, Shell's City and Hill Brothers.[4/]

3/ Securities Exchange Act Release No. 8462, 11-29-68.

4/ Rule 10b-6 (17 CFR 240 10b-6) provides in pertinent part, that:

It shall constitute a 'manipulative or deceptive device or contrivance' as used in Section 10(b) of the [Exchange Act]

(CONTINUED)

The three stocks concerned here were all "hot issues" and were all underwritten by Executive Securities Corp. ("Executive") of Miami, Florida with which Wolfson had been associated prior to forming Newport. Hot issues result where the price of a new offering of securities rises to a substantial premium over the initial offering price immediately or very soon after the securities are first distributed to the public.

Newport was a member of the selling group in connection with the public offering of the common stock of DCA on January 21, 1969, Shell's City on April 17, 1969 and Hill Brothers on May 12, 1969. The principal underwriter on these offerings was Executive and Newport received substantial allotments of these stocks.

Hill Brothers Distribution

On May 12, 1969, Hill Bros. offered and sold to the public 1,000,000 shares of its 5¢ par value common stock at $2 per share. The underwriter for the issue was Executive and Newport received 205,000 shares or about 20% of the offering. The offering was

---

4 / Continued.
for any person

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

(3) who is a broker, 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 to such distribution . . . or to attempt to induce any person to purchase any such security . . . until after he has completed his participation in such distribution . . .

oversubscribed and Newport sold its entire allotment of 205,000 shares in 802 transactions on May 12, 1969. Wolfson allocated the Hill Bros. stock to Newport salesmen based on their past production and what he described as probable "continuity of interest" of their customers. Because of this allocation of shares many customers could not purchase all that they wished to in the offering and had to buy additional shares in the after market.

On May 12, 1969 between 7:08 a.m. and 7:11 a.m. PDT, while the distribution was still going on, Wolfson and Susson sold 45,200 shares of Hill Bros. to close relatives and friends in New Jersey, Massachusetts, Pennsylvania, Florida, Maryland and California. These shares were sold at the offering price of $2 per share. Simultaneously, between 7:07 and 7:11 a.m. PDT Newport repurchased 34,700 of these shares at prices ranging from 2¼ to 2½ and sold 5,000 shares back to Executive, the managing underwriter of the new offering, and 9,000 to employees and relatives of employees at Newport at 2½. After making these sales Newport began selling the rest of the repurchased stock to other customers at 7:22 a.m. (PDT) at prices ranging from 3½ to $5 per share.

The sales to relatives and friends, made at a time when the offering was over-subscribed and customers were being allocated fewer shares than requested and being told to purchase the rest in the after-market, included 4,000 shares to Wolfson's sister, 4,000 shares to his brother-in-law, and 10,000 shares to his uncle. According to the time stamp on the order tickets the purchase of the 10,000 shares by

his uncle was at 7:08 a.m. while the sale was 7:07 a.m., which would indicate that the shares had been sold before they were actually purchased for the account. In any event they were purchased for Wolfson's uncle (Fred Finklehoffe) before payment for the shares was received, payment being made out of the proceeds of the sale of the same shares. This will be discussed in more detail under the section concerning violations of Regulation T, infra.

Wolfson's and Susson's sales of 45,200 shares of the Hill Bros. offering to accounts of close relatives and friends and Newport's simultaneous repurchase of 34,700 of said shares from such accounts prevented the offering from being completed until the resale to the public of the repurchased shares. At the same time Wolfson, Susson and Reno were inducing other persons to purchase this stock. This activity was in violation of Rule 10b-6.

The Commission has held that 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". 5/ In the instant case the Hill Bros. distribution had not been completed while shares in the offering were temporarily placed with insiders and "affiliated" persons. 6/ Accordingly, the repurchase by Newport of the 34,700 shares

---

5/ Lewisohn Copper Corp. 38 S.E.C. 26 (1958).

6/ Atlantic Equities Company Sec. Exch. Act Rel. No. 8118 pp. 9-10 (July 11, 1967); R.A. Holman & Company, Inc. Sec. Exch. Act Rel. No. 7770 (December 15, 1965), Aff'd 366 Fed. 2d 446

(CONTINUED)

from these accounts while the distribution was still going on was in violation of Rule 10b-6. Also, testimony of investors that Susson and Reno alloted shares in the Hill Bros. offering upon condition that additional purchases would be made in the after-market supports the conclusion that by this practice the respondents were inducing persons to purchase a security of the class being distributed at a time when a participant had not completed his participation in the distribution and was in violation of Rule 10b-6.

Shell's City Distribution

Shell's City was another hot issue underwritten by Executive Securities. The offering consisted of 310,000 shares of Shell's City common stock at $10.50 per share and Newport, as a member of the selling group, was allocated 70,000 shares. The offering was made on April 17, 1969, and was over-subscribed. According to the unrefuted testimony of investor witnesses Wolfson, Susson, Reno, Clymore and Fine required customers to purchase Shell's City in the after-market on April 18, 1969, as a condition for getting shares in the offering on April 17, 1969. Wolfson was taking orders from customers on April 17, 1969, for after-market sales on April 18, 1969. Reno, Fine and Clymore took orders from customers on or before April 17, 1969, for purchases in both the offering and the after-market at the same

---

6 / Continued.
(2nd Cir. 1966), modified on other grounds 377 Fed. 2d 365 (1967), Cert. denied, 389 U.S. 991 (1967); Batten & Company, Inc., 41 S.E.C. 538 (1963), Aff'd 345 Fed 2d 82 (C.A.D.C. 1964).

time. As in the Hill Bros. distribution these activities of attempting to induce and inducing customers to purchase a security of the class being distributed while still involved in the distribution of the offering constituted a violation of Rule 10b-6.

DCA Distribution

Development Corporation of America (DCA) offered 203,200 shares of its common stock at $9.50 per share on January 21, 1969. The underwriter for the issue was Executive Securities and Newport's participation was 40,000 shares or approximately 20% of the issue. Newport sold its entire participation of 40,000 shares in 325 transactions on January 21, 1969.

The record discloses that during the distribution of Newport's 40,000 share allocation of the DCA offering Dawson and Fine required customers to purchase shares in the after-market as a condition for getting shares in the offering. Dawson testified at the hearing that he did not take orders from customers for the purchase of DCA stock in the offering and subsequent after-market at the same time. This was contrary to his earlier testimony before the Commission's staff where he testified that he did take orders for the purchase of DCA shares in the initial offering and the after-market at the same time.

The activity of Dawson and Fine in inducing customers to purchase DCA while it was being distributed before Newport had completed its participation in the distribution is supported by the record and was in violation of Rule 10b-6.

Respondents state that they had no intention of influencing or manipulating the market in connection with the Hill Bros., Shell's City or DCA offerings. They claim that the events which occurred prior to the offering were an effort to accommodate customers who wanted more stock than was available and that there is no evidence that the sales and repurchases were not legitimate transactions or that people at Newport had any beneficial interest in the accounts. They argue that in the case of Hill Bros. the distribution had been completed before the after-market sales began. In advancing their contentions respondents rely primarily on their own testimony and do not offer any evidence which seriously refutes the testimony of investor witnesses.

Upon a review of the record and consideration of all of the circumstances, as discussed herein, it is found that Newport, Wolfson, Susson, Dawson, Reno, Fine and Clymore willfully violated and willfully aided and abetted violations of Section 10(b) of the Exchange Act and Rule 10b-6 thereunder, as alleged in the order for proceedings.

Excessive Mark-Ups in the Sale of Hill Bros., DCA and American Foods.

Hill Bros.

The Hill Bros. offering, described above, took place on May 12, 1969, and on the same day Newport commenced after-market trading in the shares of Hill Bros. Newport's after-market purchases on that date totalled 37,700 shares at prices ranging from 2¼ to 4. Its after-market sales on that date totalled 34,875 shares at prices

ranging from 2½ to 5. Included in such sales were the 5,000 shares sold to Executive Securities at 2½. The percentage of mark-up ranged from 11.1 to 100%.

The Commission has long held that as part of his conduct a broker-dealer is required to sell securities at prices which are reasonably related to the current market price. 7/ Excessive and unreasonable mark-ups are contrary to the duty of a broker-dealer to deal fairly with his customers and, therefore, are in violation of the anti-fraud provisions of the Federal Securities Laws. 8/

The Commission and the courts have repeatedly held that a dealer's contemporaneous cost, absent countervailing evidence, is the best evidence of the current market price for the purpose of computing mark-ups in retail transactions. 9/

Contemporaneous cost has been defined as either the price a dealer paid for stock on the same day its sales to customers were effected or if no same day purchase occurred, the price the dealer paid for the stock nearest to the date of its sales to a customer. 10/

7/ Duker v. Duker 6 S.E.C. 386 (1939).

8/ Barnett v. United States 319 Fed. 2d 340 (8th Cir., 1963).

9/ Century Securities Company Sec. Exch. Act Rel. No. 8123 p. 7 (July 14, 1967); Aff'd sub. nom. Nees v. S.E.C. 414 Fed. 2d (211 9th Cir., 1969); Mark E. O'Leary, Sec. Exch. Act Rel. No. 8361 p. 9 (July 25, 1968); Naftalin & Co., Inc., 41 S.E.C. 823 (1964).

10/ Naftalin & Co., Inc. supra; Linder Bilotte & Co., Sec. Exch. Act Rel. No. 7738 n. 4, pp. 2-3 (November 5, 1965); Investment Service Co., 41 S.E.C. 188, 196 (1962).

In computing Newport's contemporaneous cost, the purchases from customers were examined and lowest priced purchases were used against lowest priced sales of that date to arrive at the mark-ups.

DCA

As previously described DCA was a hot issue underwritten by Executive Securities and participated in by Newport which sold 40,000 shares on January 21, 1969, the date of the offering. On the following date January 22, 1969, Newport commenced after-market trading in the shares of DCA and purchased a total of 30,000 shares from Executive Securities at prices ranging from 13 to 14 and 3,000 shares from one customer at a price of 14 1/8. On the same date Newport sold a total of 34,950 shares to customers in 183 transactions at prices ranging from 13¾ to 15 per share. The mark-up ranged from 6.2% to 11%. In computing the percentage of spread and the dollar amount of profit on these transactions the method previously described concerning Hill Brothers was used, i.e. lowest priced purchases against lowest priced sales.

American Foods Inc.

American Foods Inc. ("American Foods") had a public offering of 200,000 shares of its 10¢ par value stock at a price of $3.75 per share on January 9, 1969. Executive Securities was the underwriter and Newport had an allotment of 75,000 shares which it sold January 9th, the day of the offering. Newport commenced after-market trading on January 10, 1969, with a 100 share purchase at 5 7/8. During a

three day trading period on January 13, 14, and 15 Newport purchased an additional 7,600 shares in 22 transactions from customers at prices ranging from 6 to 6½ per share. During the same three day period Newport sold 8,770 shares to its customers in 31 transactions at prices ranging from 6½ to 7¼ per share. Computing Newport's mark-ups on the basis of its contemporaneous cost, 7,700 shares were sold with mark-ups ranging from 7.7 to 16.6 per cent. In computing the percentage of mark-up the method previously described was used.

Respondents do not dispute the percentage of mark-ups as set forth above in each of the offerings nor do they offer a recomputation to show that such percentages were incorrect or had no basis in fact. Respondents state that they understand and agree that they must charge a price reasonably related to the current market price of the security. They state that as a member of the NASD they were guided by its mark-up policy which indicates that mark-ups somewhat higher than the normal 5% maximum may be justified for stocks selling for less than $10 per share.

Respondents then go on to say that the application of the 5% rule was amplified by the NASD in 1964 when it set forth seven factors to be taken into consideration in determining whether a price is reasonable. The respondents then cite three of the factors as demonstrating that the mark-ups in connection with the transactions in Hill Brothers, DCA and American Foods were not unreasonable or excessive.

The factors cited are:

(1) The type of security involved - common stocks have a higher mark-up than bonds;

(2) The price of the security - mark-ups generally increase where price decreases, even when the amount of money is substantial. Transactions in lower price securities may require more handling and justify higher spread; and

(3) The amount of money involved in a transaction - small amount of money justifies higher mark-up.

Respondents then attempt to apply these criteria to the present situation involving Hill Brothers, DCA and American Foods.

Respondents, also, point out that the Naftalin case, supra, states the rule concerning the use of contemporaneous cost applies "unless it can be shown that the dealers contemporaneous cost is not representative of the market price at the time of his sale". Respondents then urge that the reasonableness of a dealer's mark-up is not based on his cost, but rather on the market conditions which exist at the time of the transaction. Respondents then assert that in the case of Hill Bros. the price of the after-market on May 12, the day of the offering, went from 2½ at 7:07 a.m. (PDT) to 5 by 8:45 a.m. on the same day. Therefore, respondents argue, Newport's prices were clearly reasonable and any conclusion based on contemporaneous cost other than by reference to the actual market is unfair and unjust.

Respondents' arguments are without merit in view of their participation in the manipulation of the prices at which the stocks were sold, particularly in the case of Hill Brothers. The use of an artificial market price which was created by the activity of respondents, as found in their violation of Rule 10b-6, cannot be

considered as a reasonable price at which to sell stock to customers. As the Commission has said, "It is well established that it is a fraud upon customers to charge prices not reasonably related to prevailing market prices without disclosing that fact."[11/]

It is found that the percentage mark-ups described above were excessive and unreasonable and that by selling the shares of Hill Bros., DCA and American Foods at prices which included the percentage mark-ups shown above without disclosing the true nature of the market, Newport violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and that Wolfson, who had the responsibility of computing the mark-ups, aided Newport in such violations.[12/]

The Commission has found in broker-dealer revocation proceedings that mark-ups over the prevailing market of lesser percentages than were used here were fraudulent; 5% in Linder Bilotte & Co., Inc., Sec. Exch. Act Rel. No. 7738 (November 5, 1965); 5.2% in J. A. Winston & Co. Inc., Sec. Exch. Act Rel. No. 7337 (June 8, 1964); 5.4% in Powell & McGovern, Inc. 41 S.E.C. 933 (1964). The fraud lies in the failure of the broker-dealer to adhere to the implied representation that his customers will be dealt with fairly and honestly. Duker v. Duker, supra at p. 388.

---

11 / Investment Service Co., supra.

12/ Kenneth Cabot & Co., Inc. Sec. Exch. Act Rel. No. 8817, p. 6 (February 6, 1970); Mark E. O'Leary, et al., supra, at pp. 8-9.

Violation of Section 7(c)(1) of the Exchange Act and Regulation T Thereunder

The order for proceedings, as pertinent here, alleges that from about January 1969 to January 1970, Newport willfully violated and Wolfson, Susson, Reno and Clymore willfully aided and abetted violations of Section 7(c)(1) of the Exchange Act and the rules and regulations prescribed thereunder by the Board of Governors of the Federal Reserve System.

Pursuant to Section 7(c), it is "unlawful for any member of a national securities exchange or any broker or dealer, directly or indirectly to extend or maintain credit . . . to . . . any customer (1) on any security . . . in contravention of the rules and regulations which the Board of Governors of the Federal Reserve System shall prescribe . . ." As applies to brokers and dealers, the Federal Reserve Board has exercised its authority through the promulgation of Regulation T and a brief review of its applicable provisions might be helpful in understanding the nature of the violations alleged herein.

Section 4(c)(1)(i) permits a broker to effect bona fide cash transactions involving the purchase of any security by a customer in a special cash account which does not have sufficient funds for the purpose only if he does so in reliance upon an agreement accepted by him in good faith that the customer will promptly make full cash payment for the security and that he does not contemplate selling the security prior to making payment. With respect to sales Section

4(c)(1)(ii) provides that the broker in a special cash account may sell a security for a customer provided the security is held in the account or the broker is informed that the customer owns the security and the sale is in reliance upon an agreement accepted by the creditor [13/] in good faith that the security is to be promptly deposited in the account. Section 4(c)(2) provides that a broker or dealer shall promptly cancel or otherwise liquidate the transaction where a customer purchases a security in a special cash account and does not make full cash payment within 7 business days. An extension of the 7-day period may be granted by a national securities exchange, [14/] where a good faith application is made with respect to a bona fide cash transaction and "exceptional circumstances warrant such action" (Section 4(c)(6)). Section 4(c)(8) provides that unless funds sufficient for the purpose are already in the account, no security shall be purchased for or sold to a customer in a special cash account if during the preceding 90 days the customer had purchased another security in that account and for any reason whatever sold it before he paid for it in full. The sale of a security before it has been paid for has been referred to as a "free ride".

The violations of Regulation T alleged herein fall into three categories, namely, transactions which were not bona fide cash

---

13/ "The term 'creditor means any broker or dealer . . ." Section 2(b) of Regulation T (12 CFR 220.2(b)).

14/ The exchange involved here was the Pacific Coast Stock Exchange.

transactions within the meaning of Section 4(c)(1), purchases for which payments were late, as prohibited by Section 4(c)(2), and effecting purchases at a time when the account for which they were made was restricted or "blocked" by operation of the provisions of Section 4(c)(8).

THE PROCEDURES AT NEWPORT

Beginning in March 1969, the procedures for maintaining compliance with Regulation T were the responsibility of Susson. Prior to that they had been supervised by David M. Ames ("Ames") who was the comptroller and a director of Newport.

If a customer failed to pay for a security within 7 business days and no extension was granted, Susson or Wolfson made the decision as to how the transaction was to be handled. If it was a sell out, a sell order ticket was made and given to Wolfson or Susson who would initial it, execute it, and have a confirmation typed. The original confirmation was then mailed to the customer and copies were circulated internally at Newport.

If a customer purchased securities and paid for them by check, the check was deposited by Newport in its account at the Newport National Bank. If the check came back stamped NSF ("not sufficient funds"), Newport would instruct the bank to redeposit the check. If the check came back a second time marked "NSF", Newport would issue its check to the bank to cover the "NSF" check and debit the customer's account for the amount. Newport would then either cancel the trade,

sell other securities in the customer's account to pay for the transaction, or wait for the customer to send in the money. Susson or Wolfson made this decision at Newport.

The specific violations as alleged to have occurred in particular accounts are described below.

HELEN NIPPER

Helen Nipper ("Nipper") is the maiden name of Wolfson's wife. Wolfson was the account executive for the Nipper cash account at Newport and purchased stocks for her in the account.

On June 13, 1969, the Nipper account purchased 1,000 shares of Shell's City stock at $13½ for a total cost of $13,500. As of June 13, 1969 the credit balance in the Nipper account was $150. The balance of $13,350 due on this purchase was not paid by June 24, 1969 which was 7 full business days after the date of purchase of the shares. On June 24, 1969, Newport did not cancel or otherwise liquidate the unsettled portion of the transaction, as required by Section 4(c)(2). On July 1, 1969, a check for the amount of $13,350 was drawn on the account of Gurdon and Helen Wolfson at United California Bank, ("UCB") at its Laguna Beach Office and deposited in the Nipper account at Newport.

On August 6, 1969, the Nipper account purchased 5,000 shares of Instrument Tech at $8 for a total cost of $40,000. The Nipper account did not pay the $40,000 balance due on the purchase of the 5,000 shares of Instrument Tech by August 15, 1969, which was 7 full

business days after the date of the purchase of the shares. On August 15, 1969, Newport did not cancel or otherwise liquidate the transaction as required by Section 4(c)(2). On August 20, 1969 check #222 in the amount of $40,000 was drawn on the account of Gurdon and Helen Wolfson (#130-504635) at UCB, signed by Helen Wolfson, and deposited in the Nipper account at Newport to pay for the 5,000 shares of Instrument Tech. The balance in the account of Gurdon and Helen Wolfson at UCB on August 20, 1969 was $999.42.

On August 20, 1969, the Nipper account sold the 5,000 shares of Instrument Tech at $8 for a total of $40,000. On the same day, Newport issued a $40,000 check payable to Helen Nipper in order to pay the Nipper account the proceeds from the sale of the 5,000 shares of Instrument Tech. Helen Wolfson endorsed the check "Helen Nipper" and "Helen Wolfson" and on August 21, 1969, used it to buy cashier check #41692 for $40,000 which was deposited on the same day in the Gurdon and Helen Wolfson account at UCB to cover the payment of Gurdon and Helen Wolfson's check #222 which had been used to pay for the 5,000 shares of Instrument Tech and which cleared the bank on August 21, 1969. After this transaction Newport did not restrict the Nipper account for 90 days as required by Section 4(c)(8).

On September 8, 1969, the Nipper account purchased 1,500 shares of Micro Tenna at $7 for $10,500. On September 15, 1969 a check for $10,500 was deposited in the Nipper account at Newport to pay for the purchase of the 1,500 shares. On September 8, 1969 the date of the purchase of said shares, there were not sufficient funds in the

Nipper account at Newport to pay for the purchase of the shares, as required by Section 4(c)(8).

On September 12, 1969 the Nipper account purchased 2,000 shares of Shell's City stock at $8 for $16,000 when there were not sufficient funds in the Nipper account at Newport to pay for the purchase as required by Section 4(c)(8). In fact there was a debit balance of $10,500 in the Nipper account resulting from the Micro Tenna purchase described above.

With respect to the Nipper account respondents state that the purchases on June 13 and August 6, 1969 did not violate Section 4(c)(2) of Regulation T because a five day extension had been obtained from the Pacific Coast Stock Exchange. Furthermore, respondents state that the August 6 transaction did not violate Section 4(c)(8), which requires that the securities be paid for before they are sold, because Newport received a check on August 20, 1969, which would have been within the extension period, and this constituted cash payment.

There is no doubt that without the extensions these two transactions would have violated Section 4(c)(2) in that they would have been six days and three days late, respectively. Section 4(c)(6) provides for an extension by a National Securities Exchange if it is satisfied that the creditor is acting in good faith in making the application, that the application relates to a bona fide cash transaction, and that "exceptional circumstances warrant such action." However, an official of the Pacific Coast Stock Exchange testified

that registered representatives of a brokerage firm or their wives are not entitled to receive an extension of time for payment from the exchange and such extension would not have been granted in the present case if the relationship had been known. Here the five-day extensions were requested by Newport in the name of Nipper, Wolfson's wife's maiden name, with the reasons being given as "funds in the mail" and "out of town on emergency." The relationship between Wolfson and Nipper was not disclosed to the exchange.

Despite the reason for the Shell's City extension being given as "funds in the mail" on June 24, the check is dated July 1, 1969, and was deposited to the Newport account on the same date. It cleared Wolfson's account on July 3, 1969. Accordingly, some doubt is cast on the credibility of exceptional circumstances and the good faith required in making an extension application.

As to the extension involved during the August 6 purchase of 5,000 shares of Instrument Tech for a cost of $40,000 the reason given there for an extension is "customer out of town on emergency." In addition, respondents argue that under Section 6(f) of Regulation T a creditor may at his option (1) treat the receipt in good faith of any check drawn on a bank which in the ordinary course of business is payable on presentation and that this check was received by Newport on August 20, 1969, and accordingly, was properly received as cash payment.

In view of the details of the payment for the 5,000 shares of Instrument Tech as set forth on pages 20 and 21 _supra_ respondents

contention that payment was properly made within the prescribed time and in good faith is rejected. The issuance of the check when there was no money to cover it, the sale of the shares prior to payment, the subsequent issuance of a check payable to Nipper, and the purchase of a cashier's check on August 21st which was then deposited in Wolfson's account to cover the check written on August 20th all indicate an attempt to conceal the true nature of the transaction. Accordingly, it is found that in the handling of the Nipper special cash account, Newport willfully aided and abetted by Wolfson, violated Sections 4(c)(1), 4(c)(2) and 4(c)(8) of Regulation T.

GURDON WOLFSON

Wolfson was the account executive for his own cash account at Newport. On October 1, 1969 the Gurdon Wolfson ("Wolfson") account purchased 1,000 shares of AVI at $17 for $17,000. On October 10, 1969, check #393 in the amount of $17,000, signed by Helen Wolfson, [15/] and drawn on the account of Gurdon and Helen Wolfson at UCB was deposited in the Wolfson account at Newport to pay for the purchase of said shares. On October 10, 1969, the account of Gurdon and Helen Wolfson at UCB had a credit balance of $557.13.

On October 13, 1969 the Wolfson account sold the 1,000 shares of AVI at $13 for $13,000 and 2,000 shares of Instrument Tech at $6½ for $13,000. On the same day Newport issued its check #3000 to

---

15/ Wolfson testified that all checks were issued and signed by his wife.

Wolfson in the amount of $26,000, to pay him the proceeds from the sale of said shares. On October 13, 1969, check #3000 was deposited into the account of Gurdon Wolfson and Helen Wolfson at UCB to cover check #393 for $17,000 which Wolfson had used to purchase the 1,000 shares of AVI on October 10th. After this transaction, the Wolfson account was not restricted for 90 days as required by Section 4(c)(8).

On October 16, 1969, the Wolfson account purchased 1,000 shares of AVI at $13 for $13,000 when the credit balance in the account was only $500, so that the balance due on this purchase was $12,500. The Wolfson account did not pay the balance due on the purchase of the 1,000 shares of AVI by October 27, 1969 which was 7 full business days after the purchase. On October 28, 1969, $13,000 was deposited in the Wolfson account. On October 27, 1969, Newport did not cancel or otherwise liquidate the transaction as required by Section 4(c)(2).

On October 31, 1969, the Wolfson account purchased 1,000 shares of Resort Car at $12½ for $12,500 when the credit balance in the account was $500 and the account should have been restricted in accordance with Section 4(c)(8) as a result of the AVI transaction described above. On November 12, 1969, the Wolfson account sold 650 shares of AVI at $12 for $7,800 and 600 shares of Shell's City, Inc. at $7¼ for $4,350 to pay for the purchase of the 1,000 shares of Resort Car. The sale of the 600 shares of Shell's City was a short sale and was not covered until April 28, 1970 when the Wolfson account purchased 600 shares of Shell's City, Inc. at $5. On December 16, 1969, the Wolfson account

sold 400 shares of Resort Car at $11 for $4,400 and on the same day Wolfson was paid $4,400 by Newport. On January 26, 1970, the Wolfson account sold 300 shares of Resort Car at $7½ for $2,250.

On May 4, 1970, the Wolfson account purchased 10,000 shares of General Rest Homes for $7,950. On May 12, 1970, the Wolfson account sold 4,000 General Rest Homes at $1½ for $6,000. On May 13, 1970, check #320 in the amount of $7,950 was drawn on the account of Gurdon and Helen Wolfson at UCB, signed by Helen Wolfson and deposited in the Wolfson account at Newport to pay for the 10,000 shares of General Rest Homes. On May 18, 1970, Newport paid Wolfson the $6,000 proceeds from the sale of the 4,000 shares of General Rest Homes on May 12, 1970 by its check #5022 and on the same day Wolfson deposited said check in his account at UCB to cover his check #320 which cleared UCB on May 20, 1970.

Respondents state that the purchase of 1,000 shares of AVI in Wolfson's account on October 1, 1969 was paid for by check on October 10, 1969 and therefore was not in violation of Regulation T because the check is acceptable as payment under 6(f) of Regulation T. What respondents fail to take into account is that the same "free riding" technique utilized in the Nipper transaction was also resorted to here in that the Wolfson check deposit as of October 10, 1969 was not collectible until made good by the receipt of the proceeds from the sale of the same shares on October 13, 1969. This continued use of form over substance indicates a lack of the good faith called for in the handling of special cash accounts under both Sections 4(c)(1)

and 6(f) of Regulation T. Accordingly, it is found that this was a violation of Section 4(c)(1) of Regulation T and that the account should have been restricted in accordance with the requirements of Section 4(c)(8) of Regulation T.

Respondents admit that the transaction on October 16, 1969 should have been paid for on October 27, 1969 and that the payment which was made on October 28, 1969 was one day late. Thus they do not dispute that this was a violation of Section 4(c)(2) of Regulation T.

Respondents do not address themselves to the purchase in the Wolfson account on October 31, 1969, when, in view of findings made above, the account should have been restricted in accordance with 4(c)(8) of Regulation T. As set forth above payment for the October 31st transaction was made, in part, through the short sale of 600 shares of Shell's City stock.

The Federal Reserve Board has long since made clear -- as the language of Section 4(c)(1)(ii) unambiguously indicates -- that from the broker's view point sales effected in a special cash account must be treated as "long" sales; "the making of a short sale by a customer in a special cash account is forbidden." 25 Fed. Res. Bull. 466 (1939).

In this transaction, Wolfson, acting for his own account, was on both sides of the transaction so that there can be no doubt that he was aware that it was not a bona fide cash transaction as required by Section 4(c)(1) of Regulation T.

The transaction of May 4, 1970, concerning General Rest Homes stock, while occurring outside of the period charged in the order nevertheless is an indication of the continuing violations engaged in by Wolfson and Newport and illustrates respondents' disregard of their responsibilities in the operation of a brokerage business.

RICHARD S. WOLFSON & J. LEONARD DIAMOND

Richard S. Wolfson ("R. Wolfson") is Wolfson's brother and resides at Miami Beach, Florida. R. Wolfson was a customer of Wolfson at Newport and had transactions with Wolfson through a cash account entitled Richard S. Wolfson and J. Leonard Diamond tenants in common w/o rights of survivorship ("W&D").

On February 12, 1969, the W&D account purchased 500 shares of Aero Tech at $25 for $12,500. On February 14, 1969, the W&D account purchased 500 shares of Aero Tech at $26 for $13,000. Check #181 drawn on the W&D Investment Account at the Mercantile Bank, Miami Beach, Florida, in the amount of $25,500 was deposited in the W&D account at Newport on February 26, 1969 to pay for the purchase of the 1,000 shares of Aero Tech.

On March 5, 1969, check #181 was returned to Newport's Bank by the Mercantile Bank marked NSF. On March 5, 1969, Newport did not cancel or otherwise liquidate the transactions whereby the W&D account purchased the 1,000 shares of Aero Tech, as required by Section 4(c)(2). Check #181 was redeposited by Newport's bank and on March 18, 1969 it was again returned from the Mercantile Bank

marked NSF. On March 24, 1969, Newport paid Newport National Bank two checks totalling $25,500, signed by Wolfson and Susson, to cover the "NSF" check and debited the W&D account at Newport for that amount. On March 27, 1969, before paying the $25,500 due on the purchase, the W&D account sold the 1,000 Aero Tech at $13 for $13,000. After this transaction, Newport did not cancel or otherwise liquidate the transaction, as required by Section 4(c)(2). The W&D account at Newport was not restricted for 90 days, as required by Section 4(c)(8).

On March 11, 1969, the W&D account purchased 1,500 shares of Micro Tenna at $16¼ for $24,375. On March 11, prior to the purchase of said shares, there was a credit balance in the W&D account of $8,500. On March 18, 1969, the W&D account sold 1,000 of the Micro Tenna shares at $22 for $22,000. On March 20, 1969, check #182 was drawn by the W&D Investment Account on the Mercantile Bank in the amount of $15,875 and was credited to the W&D account at Newport on March 21, 1969. On March 21, 1969, the W&D Investment Account at the Mercantile Bank did not have sufficient funds in it to cover check #182. On March 24, 1969, Newport paid R. Wolfson and J. Leonard Diamond $15,875, the credit balance in the W&D account at Newport due from the sale of the 1,000 shares of Micro Tenna. The W&D account deposited the Newport check for $15,875 in its account at the Mercantile Bank and used it to cover its check #182 which had been issued to Newport to pay for the purchase of the 1,500 Micro Tenna and which cleared the Mercantile Bank on March 28, 1969. Following this transaction the W&D account was not "blocked" or

"restricted" for 90 days as required by Section 4(c)(8).

On April 24, 1969, the W&D account purchased 2,000 shares of Shell's City. On April 29, 1969 this transaction was cancelled as of April 24, 1969 and a purchase was made of 2,000 shares of Shell's City at $13½ for $27,000 as of April 29, 1969. With a credit balance in the account of $62.50, the W&D account owed Newport $26,937.50 for the purchase. On May 12, 1969, $26,937.50 was deposited into the W&D account at Newport by check #190 which was drawn on the W&D Investment Account at the Mercantile Bank. On May 12, 1969, there were not sufficient funds in the W&D account at the bank to cover payment of check #190. On May 19, 1969, Newport debited the W&D account for $26,000 and paid its bank $26,000 by check #1187 signed by Dawson and Susson. Newport's Bank then sent the $26,000 by wire to the Mercantile Bank on the same day and the $26,000 was credited to the W&D Investment Account at said Bank and used to clear check #190 for $26,937.50.

Respondents state that a three-day extension was obtained for the W&D account for the February 12th transaction so that the due date was February 26, 1969 and, therefore, Section 4(c)(2) of Regulation T was not violated. The respondents go on to present the same defense concerning transactions in the W&D account as they did in the Nipper and Wolfson accounts, which is that payment is presumed to be good when the check is received by Newport even though as in this case the checks were returned time and again marked NSF and payment had to be made finally by selling some of the securities

in the account before they had been paid for. Respondents also state that they do not have any idea as to why $26,000 was paid to the account by Newport on May 19, 1969. This apparently was an advance or a loan by Newport to W&D for the purpose of clearing the W&D check for $26,937.50 deposited at Newport on May 12, 1969, at a time when there were not sufficient funds in the W&D account at its bank to cover payment of the check.

The transactions in the W&D account as previously detailed at pages 28-30 supra are found to have been in violation of Sections 4(c)(1), 4(c)(2) and 4(c)(8) of Regulation T.

FRED F. FINKLEHOFFE

Fred F. Finklehoffe ("Finklehoffe") is Wolfson's uncle and resides at Springtown, Pennsylvania. Wolfson handled Finklehoffe's cash account at Newport.

On May 12, 1969, Finklehoffe purchased from Newport 10,000 shares of Hill Bros. at $2 per share in the offering. At the time of the purchase there were no funds in the Finklehoffe account. On the same day, Finklehoffe sold the 10,000 shares of Hills Bros. to Newport at 2¼ per share and received a check from Newport for $22,500 which was post-dated May 14, 1969 and signed by Wolfson and Susson. Also, on the same day, Finklehoffe took the $22,500 check from Newport and went to the UCB, Laguna Beach Office and opened a checking account, #130-104699, depositing the $22,500 check in the checking account. On the same day Finklehoffe drew a check for $20,000 on the checking account and gave said check to Newport to pay for the 10,000 shares

of Hill Bros. which he had just purchased and sold. After crediting Finklehoffe's account, Newport deposited his $20,000 check at Newport National Bank on May 12, 1969. Finklehoffe had no other accounts or transactions with UCB, Laguna Beach.

The Finklehoffe transaction as set forth above is a classic example of a "free ride" and was in violation of Section 4(c)(8) of Regulation T. It also was not a bona fide transaction and violated Section 4(c)(1) of Regulation T. This transaction was particularly flagrant in view of the fact that it not only violated Regulation T but, also, served to further the manipulation described under the Hill Bros. offering, page 6 supra, which in turn violated Section 10 of the Exchange Act and Rule 10b-6 thereunder.

MIKE FRANKEL

Mike Frankel ("Frankel") had a cash account with Wolfson at Newport. On September 15, 1969, the Frankel account purchased 400 shares of Shell's City at $8½ for $3,400. On September 22, 1969, the Frankel account at Newport was credited with a deposit of $3,400. However, Frankel's check was returned marked NSF and on October 8, 1969, Newport paid its bank $3,400 and debited the Frankel account at Newport for that amount. On October 8, 1969, the Frankel account sold 50 shares of American Food at $4 for $200 and 400 shares of Shell's City at $8 for $3,200 to cover the $3,400 debit in the account. The 400 shares of Shell's City were the same shares that the Frankel account had purchased on September 15, 1969 and paid for with the check which was returned marked NSF.

The Frankel account was marked restricted 90 days from September 15, 1969. However, on October 23, 1969, the Frankel account purchased 500 Imperial Industries at $8 for $4,000. At the time of the purchase of those shares there were not sufficient funds in the Frankel account at Newport to cover the purchase as required for accounts restricted pursuant to Section 4(c)(8). On November 7, 1969, the Frankel account sold short 800 shares of Hill Bros. at $5 for $4,000 in a purported attempt to cover the purchase of 500 shares of Imperial Industries on October 23, 1969.

Respondents admit that the Frankel account was not in compliance with Regulation T on October 8, 1969, on a September 15, 1969 transaction; that the account was sold out and was marked restricted 90 days from September 15, 1969. Respondents admit further that the Frankel account engaged in another transaction on October 23, 1969 which would have been in violation of Section 4(c)(8) of Regulation T. However, respondents state that securities were sold out on November 7, 1969 to cover this transaction and the ledger card was then marked "restricted 90 days from 11-7-69". Respondents state that Regulation T makes specific provision for innocent mistakes and state that a creditor shall not be deemed in violation if he takes remedial action. Respondents urge that an oversight occurred here and that it was corrected when discovered.

Respondents naive statement that this was nothing more than an oversight is not acceptable. Newport demonstrated by restricting the account in accordance with Section 4(c)(8) of Regulation T that

it was fully cognizant of the requirements of Regulation T. However, in spite of this, a violation was permitted to occur. Further, what respondents do not disclose when they state that securities were sold to cover this transaction is that this was a short sale which as discussed previously, is prohibited by Section 4(c)(1)(ii) of Regulation T. Accordingly, it is found that this transaction violated Sections 4(c)(1) and 4(c)(8) of Regulation T.

YOST, STEPHENS, AND BECKLUND ACCOUNTS

ROGER YOST

Roger Yost ("Yost") had a cash account with Wolfson at Newport. On August 14, 1969, the Yost account purchased 100 shares of AVI at $17 for $1,700. On August 25, 1969, which was 7 business days after date of purchase, $1,700 was deposited in the Yost account at Newport. However, Yost's check for $1,700 was returned "NSF" twice and on September 10, 1969, Newport paid its bank $1,700 to cover it and the Yost account was debited for that amount. Newport did not cancel or otherwise liquidate the transaction either time the check was returned "NSF", as required by Section 4(c)(2), and Yost's account was not restricted for 90 days, as required by Section 4(c)(8). On September 25, 1969, Yost deposited $1,700 in his account at Newport.

CHARLES STEPHENS & MARY O. STEPHENS

Charles E. Stephens and Mary O. Stephens ("Stephens") had a cash account with Clymore at Newport in 1969. On February 12, 1969, the Stephens account purchased 50 shares of Aero Systems at $21 3/4

for $1,087.50 and when payment was not made they were sold by Newport on February 24, 1969, as required by Section 4(c)(2), at 17¼ for $862.50, leaving a debit balance of $225 in the account. However, the Stephens account was not restricted for 90 days from February 12, 1969, as required by Section 4(c)(8).

On February 26, 1969, the Stephens' account purchased 100 shares of Hydro Tech at $6¼ for $625, 50 shares of Aero Systems at $18 for $900, and 30 shares of Hydro Tech at $6¼ for $187.50, a total of $1,712.50. There were not sufficient funds in the Stephens account on February 26, 1969 to pay for these purchases. On February 28, 1969, $1,087.50 was deposited in the Stephens' account; on March 1, 1969, the account was credited with $37.50, and on March 6, 1969, $650.63 was transferred into the account from the Mary O. Stephens account leaving a debit balance of $161.87 in the Stephens account on that date.

On March 26, 1969, the Stephens account purchased 50 shares of Instrument Tech at $14 for $700 when there were not sufficient funds in the account to pay for this purchase. On March 26, 1969, $712.75 was transferred into the Stephens account from the Mary O. Stephens account, leaving a debit balance in the Stephens account of $149.12. On March 27, 1969, the Stephens account was credited with $149.12 which amount was deducted from commissions owed to Clymore by Newport. The Stephens account was not restricted for 90 days after this transaction, as required by Section 4(c)(8).

JANET BECKLUND

Janet Becklund ("Becklund") had a cash account with Reno at Newport in 1969. On March 19, 1969, the Becklund account purchased 100 shares of AVI at $31 for $3,100 and with a credit balance in the account of $2,981.29, it owed Newport $118.71. The debit balance of $118.71 was not paid by March 28th, which was seven business days after March 19, 1969, and the unsettled portion of the transaction was not cancelled or otherwise liquidated as required by Section 4(c)(2). On April 1, 1969, Reno deposited $118.71 into the Becklund account.

Respondents do not seriously dispute the violations in these accounts as set forth above. They submit that they are isolated violations which appear to be technical in nature and are obviously not willfull or grevious.

On the basis of the facts previously stated it is found that the transactions in the Yost and Stephens accounts violated Sections 4(c)(2) and 4(c)(8) of Regulation T and the transaction in the Becklund account violated Section 4(c)(2). The violations in the Stephens and Becklund accounts were participated in by Clymore and Reno, respectively, inasmuch as cash payments to the account must be made by the customer and not by the securities salesman.

It is apparent from the numerous and extensive violations of Regulation T which have been found herein that the procedures at Newport for enforcing Regulation T were not effective and that no serious effort was made to comply with the enforcement of the

Regulation and that the violations were clearful willful.[16/]

Moveover, the violations of Regulation T found herein were particularly opprobrious in that they were not, for the most part, the ordinary late-payment type involving arms-length transactions between broker and customer but, rather, were part of an arrangement by Wolfson to trade in securities without risk on the part of Wolfson, his wife, relatives and friends by purchasing securities and then selling the same securities to pay for their purchase. This activity was concealed by exchanging checks of like amounts, using a cashier's check, post-dating a check, issuing Newport's checks (signed by Susson) to customers for the proceeds of sales of securities before the securities had been paid for, and charging a salesman's commission account for payment due from a customer.

Accordingly, it is found that Newport, willfully aided and abetted by Wolfson, Susson, Clymore and Reno violated the provisions of Section 7(c) of the Exchange Act and Regulation T thereunder.[17/]

16/ Coburn and Middlebrook, Inc. 37 S.E.C. 583 (1957); Schweickart & Co., Sec. Exch. Act Rel. No. 7623 p. 3 (June 8, 1965).

17/ Sutro Bros. & Co. 41 S.E.C. 443 (1963); V. Lester Yuritch Sec. Exch. Act Rel. No. 7875 (April 28, 1966); Naftalin & Co. Inc. et al. 41 S.E.C. 823, 831-832 (1964).

Violations of the Anti-Fraud Provisions Under the Securities Acts

The order for proceedings alleges that from January 1, 1969 to January 31, 1970, Newport, Wolfson, Susson, Dawson, Reno, Fine, Clymore and Harrison, singly and in concert, willfully violated and willfully aided and abetted violations of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act [18/] and Rule 10b-5 thereunder in connection with the offer and sale of the common stock of various companies as will be described hereunder.

During the period here relevant over 98 percent of Newport's business was in over-the-counter stocks, exchange listed securities being handled on an agency basis only as a convenience to customers. In the first six months of 1969, over 90 percent of Newport's customer retail business was over-the-counter principal business and approximately 85 percent of that was in stocks secured through Executive Securities Corp., Miami, Florida, ("Executive") with which Wolfson had been associated prior to forming Newport.

Wolfson was the trader at Newport and executed all over-the-counter principal transactions. Each morning he prepared a list of

---

18/ Section 10(b) as here pertinent makes it unlawful for any person to use or employ in connection with the purchase or sale of a security any manipulative device or contrivance in contravention of rules and regulations of the Commission prescribed thereunder. Rule 10b-5 defines manipulative or deceptive devices by making it unlawful for any person in such connection: "(1) to employ any device, scheme, or artifice to defraud, (2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or (3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person . . . ." Section 17(a) contains analogous antifraud provisions.

stocks with their bid and asked prices and had them placed on the salesmen's desks. These were the stocks which the salesmen were instructed to recommend to customers and stocks not on the list were not to be recommended. A larger commission was paid for selling the listed stocks than for selling non-listed ones. The solicitation and selling was done almost entirely by telephone.

The record discloses that from January 1, 1969 to January 31, 1970 Newport was actively recommending on a day-to-day basis 10 of the thirteen stocks named in the order. Thirty-three investor witnesses testified during the hearing as to their purchases of these stocks and the representations made to them which induced them to make such purchases.

Representations by Salesman

Wolfson

Wolfson was the largest producer at Newport and six investors testified concerning transactions with him in six of the stocks named in the order.

Mr. S., a school teacher, testified that he opened an account with Wolfson at Newport on the suggestion of a friend. At the time he told Wolfson that he was salaried with a limited income, a conservative investor who wished to be careful regarding stock purchases. In early 1969 Wolfson told S about Micro Tenna which he said had an antenna system which was going to revolutionize the aviation field and other areas such as small boats. Wolfson told S that Micro Tenna, which was then selling at $16 a share, would rise to somewhere between $50 and $60 a share and then be split because of

the small amount of stock outstanding, 60,000 shares. Wolfson stated that the downside risk was negligible. Based on Wolfson's recommendations, S bought 650 shares of Micro Tenna at 16¼ on March 11, 1969.

As a matter of fact, Micro Tenna had been spun-off from Aero Systems in late 1968 and at the time it was being sold by Newport in 1969 it was an unseasoned company still in the research and development stage and highly speculative. It had not completed the development of the antenna and was not manufacturing it. It was not in operation and had no earnings. None of this was disclosed to S by Wolfson.

Wolfson called S in the spring of 1969 and told him about a company called Hill Brothers, Inc. ("Hill Bros.") which had an initial offering of 1,000 shares at $2.00 a share on May 12, 1969. This was a hot issue as more fully described herebefore. Wolfson encouraged S to buy the stock at $2 a share in the offering and predicted that the price would go to $20. and that S would do well with it. Based on Wolfson's recommendation, S bought 1000 shares at $2 in the offering on May 12, 1969. Wolfson continued to call S and urge him to buy additional shares and on May 15, 1969, S purchased another 1,000 shares at 4½. Later, when the stock was at $5, Wolfson called S and told him that the price of the stock was acting just as he had predicted and urged him to buy more. S bought an additional 300 shares of Hill Bros. at $5 a share on July 11, 1969.

In 1969 Hill Bros. located in Miami, Florida, was in a highly competitive business of wholesaling a line of grocery items,

competing against grocery groups, co-ops and grocery chains such as Winn-Dixie, Food Fair, A & P and Grand Union. For the 44 week period ended March 1, 1969 the company earned $70,104 or $.04 a share compared to $48,575, or $.03 a share for the comparable period in 1968. S cannot recall receiving any financial information.

In early 1969 Wolfson recommended the stock of Development Corporation of America ("DCA") to S. S testified that Wolfson told him the company was doing well and the stock of other companies in the same business as DCA was selling around thirty times earnings and that DCA should be selling for $40 and would reach that figure within 90 days. Wolfson assured S that the downside risk was negligible. Acting on Wolfson's recommendation S purchased 75 shares of DCA on March 11, 1969 at $19 a share.

In 1969 Wolfson called S on the telephone and told him about a company called Shell's City, Inc. ("Shell's City"). Wolfson told S that the company had a large supermarket in the Miami area, liquor stores and places where drinks are sold on the premises and that it also had landholdings in the Miami area which were going to be used for urban renewal. Wolfson stated that the company was a substantial one and in very good shape financially without giving any specific figures. He did not indicate any negative factors nor any downside risk in buying this stock. Based on Wolfson's recommendation S bought 400 shares of Shell's City at 10½ on April 17, 1969.

In 1969 Wolfson recommended Instrument Technology Corporation ("Instrument Tech"). S testified that Wolfson was very bullish on

the company and indicated that the price of the stock would definitely go up. Wolfson told S that there was very little downside risk in buying this stock. Based on Wolfson's recommendation S bought 100 shares of Instrument Tech at $13 on March 13, 1969. Wolfson failed to disclose to S that Instrument Tech had no contracts for the instrument system it was developing and that it was losing money.

Mr. K testified that in early 1969 Wolfson called him and told him about Instrument Tech. He told K that Instrument Tech was developing an instrument system and negotiating contracts. Wolfson said that it also had a new product that could go over very strong. Wolfson compared the price appreciation potential of Instrument Tech with other stocks and stated that Instrument Tech would go to $100 but that he Wolfson, would get K out at $50. Based on Wolfson's recommendation K bought 300 shares of Instrument Tech at $13 on March 13, 1969. Wolfson told K that he should buy 1,000 shares of Instrument Tech because there was a great opportunity to make a lot of money. K later called Wolfson to sell the stock but was told not to sell it because it would be a mover and that he should hold a minimun of 1,000 shares. On the basis of this further recommendation K bought another 300 shares of Instrument Tech at 11½ on April 9, 1969. Wolfson failed to disclose anything about the financial condition of Instrument Tech.

In early 1969 Wolfson called K and told him about a secondary offering of the stock of Shell's City. Wolfson stated that the company was in the business of liquor distribution and warehousing of food in Florida, and was expanding and becoming very large. He also stated that there would be a merger between Shell's City and another

company and that the profits would be enormous and that the stock would be a winner. Based on Wolfson's recommendation K bought 100 shares of Shell's City at 10½ on April 17, 1969.

In early 1969 Wolfson recommended Micro Tenna to K telling him that Micro Tenna had acquired the patent rights to a revolutionary high frequency antenna and that they expected to get FAA approval for it. Wolfson also stated that the antenna would be applicable to television stations, boats, cars and a great many other areas and would be a very big thing. Wolfson stated that the price of the stock would be selling for at least $100 a share in a very short time. Based on Wolfson's recommendation K purchased 200 shares of Micro Tenna at 17½ on March 11, 1969.

In late 1968 or early 1969 Wolfson recommended American Foods, Inc. ("American Foods") as an exceptional situation because the company was going places. Based on Wolfson's recommendation K bought 200 shares of American Foods at 7½ on January 24, 1969.

K. testified that whenever he tried to sell stocks to Newport he was discouraged from selling and was encouraged to buy something else. When he wished to sell his American stock he had to go to another broker dealer. During the time K was purchasing stocks through Wolfson he gave instructions to have the shares delivered to his bank against due bills also delivered to the bank by Newport. This stock would be held by the bank as collateral until payment. On several occasions the stock was not delivered to the bank but was delivered out to K. The first time this happened K called the bank to get it straightened out and the second time he called Wolfson. Wolfson suggested to him that since K had

the stock and not the bank, he could raise additional monies on the stock as collateral in the interim before the bank requested the stock.

Another customer of Wolfson's Dr. C testified that in April 1969 he received a call from Wolfson concerning an offering of Shell's City. Wolfson stated that the price of the stock would rise rapidly because Shell's City was going to enter into mergers and that the present earnings of Shell's City were good. Dr. C indicated that he wanted some shares in the offering and Wolfson told him that the offering was oversold and in order to get 75 shares at the offering price he would have to buy more shares in the aftermarket. Dr. C purchased 75 shares at 10½ on April 17, 1969 and on April 18, 1969 he purchased 350 shares at 15. Dr. C testified that he did not receive the Shell's City prospectus at the time of his purchase. Wolfson indicated to Dr. C that Shell's City was a good investment at both 10½ and $15 a share and on May 15, 1969 he purchased another 1,000 shares of Shell's City at 10½ because Wolfson recommended that he buy more at that price because it was going up again.

In May 1969 Wolfson recommended Hill Brothers saying the price of the stock would rise rapidly. Wolfson also stated that the company might have a merger in the near future. On May 12, 1969 Dr. C purchased 1,000 shares of Hill Bros in the offering of $2 a share. This was ordered before he received the Hill Bros prospectus.

Another investor Mr. A testified that Wolfson recommended DCA to him and told him it was a land development company in Florida

which had good prospects for growth and development. On March 3, 1969 Mr. A purchased 200 shares of DCA at 18½.

Wolfson called Mr. A and told him that Instrument Tech was a stock that he could make money with since it would go up in value and was a growth situation. Wolfson did not describe the financial situation of the company and Mr. A did not receive any literature on the company. On March 13, 1969 Mr. A purchased 200 shares of Instrument Tech at $12.

In May 1969 Wolfson called Mr. A concerning the stock of Hill Bros. Wolfson made a strong recommendation that Mr. A buy some shares at the offering. Mr. A told Wolfson he would have to consider it. Later Mr. A received a confirmation in the mail reflecting a purchase by him of 200 shares of Hill Bros. on May 12, 1969 which he had not ordered. Accordingly,he returned the confirmation to Newport with a notation that he had not ordered the stock.

Mrs. T,who was a registered representative at Newport from late January to the end of March 1969,testified that after she left Newport she had asked Wolfson if she could purchase some shares in the Shell's City offering. Wolfson said that she could but that she would have to buy some shares in the aftermarket as well. On April 17, 1969 Mrs. T purchased 200 shares of Shell's City at 10½ in the offering and on April 18, 1969 she purchased 200 shares at 15 in the aftermarket.

Mr. G testified that up to 1969 he had never invested in any stocks and that a friend of his recommended that he purchase stocks from Wolfson at Newport. Mr. G received a confirmation in the mail

from Newport indicating that he had purchased 200 shares of Hill Bros. at $2 a share on May 12, 1969. Mr. G testified that he had never spoken to anyone at Newport about the Hill Bros stock and had never ordered the Hill Bros. Stock. In June 1969 Mr. G received a confirmation in the mail indicating that Newport had cancelled "as per Reg T" Mr. G's purchase of the 200 shares of Hill Bros.

Martin Susson

Next to Wolfson, Susson was the largest producer of business at Newport. During 1969 he recommended six of the stocks listed in the order to five investor witnesses who testified concerning the representations he made to them in recommending that they purchase the stock.

Susson was a patient of Dr. A.C., a dentist, who testified that in the Spring of 1969 Susson told him that Aero-Tech was spinning off a company called Instrument Tech. Instrument Tech was then going to take over a third company that was producing an altimeter and Susson told Dr. A.C. that the stock of Instrument Tech was going to the the hit of the year, was going to go to $30 and that there was no risk involved in purchasing it. Susson did not tell him anything about the financial condition or earnings of the company. As a matter of fact Instrument Tech was an unseasoned company still in research and development and its stock was highly speculative. Instrument Tech had lost money from the time it was spun-off by Aero-Tech in 1968 through the end of 1969. Instrument Tech was developing a system for aeroplanes and needed substantial orders in order to make a profit, but the instruments were being rejected in the Spring of 1969 as fast as they were being delivered and the overall manufacturing was so expensive that the company could not compete in the field. In June 1969 this particular instrument project was cancelled because it wasn't progressing as anticipated. None of this information was disclosed to Dr. A.C. by Susson.

Dr. A.C. testified that Susson also indicated that he was buying the stock as gifts for his relatives. Based on Susson's recommendations Dr. A.C. purchased 200 shares of Instrument Tech at 13 on March 13, 1969. Susson recommended that Dr. A.C. make a second purchase telling him it was the safest stock on the market and that it was going to go to 30 before the end of the year. Susson indicated again that he was purchasing the stock for the account of his relatives as gifts. Based on these additional recommendations Dr. A.C. purchased an additional 1,000 shares of Instrument Tech at $12 on June 27, 1969. Later when Dr. A.C. attempted to sell his Instrument Tech stock Susson attempted to talk him out of doing so but Dr. A.C. insisted and sold the stock.

Another investor Mr. J., a retiree, testified that Susson recommended Instrument Tech to him in June 1969 telling him substantially the same things that he had told to Dr. A.C. as described above. Based on Susson's recommendation Mr. J. purchased 500 shares of Instrument Tech at $12 on June 27, 1969. He was not given any written information on Instrument Tech nor was he informed of the financial condition or earnings of the company.

Mr. J. told Susson that he was accumulating funds to repay a $10,000 bank loan and Susson convinced him to use the funds to purchase Instrument Tech stock telling him that he would be able to resell the stock with a profit in time to repay the loan.

In 1969 Susson recommended Imperial Industries, Inc. ("Imperial Industries") to Mr. J. who purchased 300 shares on October 23, 1969 at $8 per share. Shortly thereafter Susson told Mr. J. that Imperial Industries stock was not going anywhere and it would be wise to sell it and buy shares of Instrument Tech in order to average down his cost of that stock. Susson told Mr. J. that Instrument Tech was still going to go to $20 a share, the figure he had originally mentioned, and that he Susson was still buying it. Based on this recommendation Mr. J. sold his 300 shares of Imperial Industries at 8½ and purchased 350 shares of Instrument Tech at 7¼ on October 30, 1969.

Another customer of Susson's, Dr. S., testified that in May 1969 Susson called him on the phone and told him that Hill Bros. was coming out with a new issue and that he could get 500 shares of the new issue if he bought 300 more shares in the aftermarket. Dr. S. ordered the Hill Bros. shares in the offering and the aftermarket at the same time. Susson had told him that the offering price would be $2 per share and the aftermarket price would be higher. On May 12, 1969, 500 shares of Hill Brothers were purchased at $2 in the offering and 300 shares were purchased at 4¼ in the aftermarket for the account of Dr. S.

In January 1969 Susson recommended International Book Corporation ("International Book") to Dr. S. telling him that the company had the only acceptable text for the history and development of the black race and the stock was going to grow because of the demand for the books. Susson told Dr. S. that International Book

was a $25 stock and would be selling at the price at a short period of time. Dr. S. purchased 500 shares of International Book at 19 3/4 on January 10, 1969.

In 1969 during the period when the respondents were selling the stock of International Book the company was engaged in the business of publishing and distributing educational material. For its fiscal year ended December 30, 1968 the company lost $1,576,217, this included losses from operations of $486,982 and extraordinary losses $1,089,525. None of this information was given to Dr. S. at the time Susson was recommending it to him as a good purchase.

Another investor witness Mr. D. was a student at UCLA in 1970 and on January 9, 1970 Susson spoke to him about Aero System, Inc. (Aero Systems). Susson told him that it was a good stock, the company was in the black, the company was going to issue 300,000 shares, and the stock would go to $10 within six months. D. asked Susson for literature on the company and on January 10, 1972 he received the literature. D. then called Susson and said that he was not interested in buying any stock in Aero Systems. On January 12, 1970, Susson again called D, repeated to him the previous information concerning Aero Systems and told him that Aero Systems stock was selling at $7¼ and that if he did not buy quickly he would have to pay $8 for it. D. purchased 800 shares of Aero Systems at 7¼.

On January 12, 1970 Susson sold to Newport 1000 shares of Aero Systems at 6 3/4 from his own account. Susson did not disclose this transaction to D. when he recommended that D. buy the Aero Systems stock. Also on January 22, 1970 Susson sold another 300 shares of Aero Systems at $6 from his own account.

Aero Systems was engaged in the aviation electronics supply business and for its fiscal year ended February 28, 1970 had a net loss from operations of $410,000 and extraordinary losses of $520,000. No financial information concerning the condition of Aero Systems was given to Mr D.by Susson.

One week after his purchase of the Aero Systems stock D. called Susson to sell the stock and was told that a financial report on the company was coming out in 10 days. D. eventually sold his Aero Systems stock against the advice of Susson.

On or about April 15, 1969, Susson told Mr. G., a retired California resident, that Shell's City was coming out with a secondary offering at $10 or $11 a share, that he had high hopes and that it was a good buy. Mr. G. asked Susson if he could get 200 shares in the offering and Susson told him that the market was tight and that he would have to buy 100 shares in the after market in order to get 100 shares in the offering. Thereupon G. ordered 100 shares in the offering and 100 shares in the after market at the same time on April 15, 1969. Susson purchased for the G. account 100 shares of the offering on April 17, 1969 and 100 shares on the after market on April 18, 1969.

Roy O. Dawson

Five investor witnesses testified concerning their purchases of stocks from Dawson. Their testimony covered the stocks of six of the companys named in the order and the representations made to them by Dawson were similar in many respects to the representations made by Wolfson, Susson and other Newport salesmen in the retailing of the stocks named in the order.

Mr. B., a retired land surveyor, had an account with Dawson at Newport during 1969. Mr. B. testified that he dealt with Dawson because he had faith in him and gave him the impression that all stocks he (Dawson) sold to him did not involve any risk

Dawson called B. in January 1969 and told him about DCA which he said was a real estate investment company in Florida. Dawson also stated that DCA was going to be a terrific growth stock and was going to go up terrifically in price and that B. would make money on it. Based on Dawson's recommendations, B. purchased 100 shares of DCA in the offering at 9½ on January 21, 1969. Dawson did not inform B. about the earnings or financial condition of DCA and B. did not receive any literature regarding DCA before he purchased the stock in the offering. Dawson did not tell B. that there was any risk involved in purchasing DCA. Later, on the same day, January 21, 1969. B. had a conversation with Dawson at which time Dawson recommended he buy another 100 shares of DCA at $15. During this conversation Dawson gave B. the feeling that he was obligated to purchase an additional 100 shares due to the fact that he had gotten 100 shares at the offering price of 9½ Accordingly B. purchased 100 shares of DCA at $15 on January 22, 1969.

On or about April 17, 1969 Dawson called B. and told him that Shell's City was having a public offering of its stock. Dawson took an indication of interest from B. before the offering became effective but did not call B. back to confirm the order before it was executed. On April 17, 1969 Dawson purchased 50 shares of Shell's City at 10½ for the B. account. Dawson did not tell B. anything concerning the financial condition or earnings of Shell's City and B. did not receive any literature from Newport prior to his purchase.

Early in 1969 Dawson called B. and told him that Instrument Tech stock would go up and that it was "going to be a big, big thing".Based on Dawson's recommendation B. purchased 100 shares of Instrument Tech on March 18, 1969 at 13½. He did not receive any literature concerning Instrument Tech before he purchased the stock and Dawson did not tell him anything about the financial condition or earnings of the company.

Investor D. testified that in January 1969 Dawson recommended that he purchase 100 shares of DCA at 9½ and that the price of the stock would go up several points. Dawson also told him that it was customary to back up the first purchase with another one a few days later after the market had gone up.

D. said "I don't know about that" and let it go at that. However, D. received a confirmation in the mail reflecting a purchase on January 22, 1969, of 100 shares of DCA at 15 which he had not ordered. This purchase was executed by Newport at 9:41 a.m. on January 22 and this time was after that at which several principals

and employees of Newport and their relatives had purchased DCA at lower prices.

Investor witness W. testified that he had told Dawson that he was interested in speculative stocks although he did not know anything about them. Dawson recommended Hill Bros. and predicted that by the end of the year the price of the stock would be $20 to $25 per share, When W. said that he was interested, Dawson stated that the offering was going so well he did not know whether he could get him any. However Dawson called him later and told him he could have 50 shares in the offering on May 12, 1969 at $2 a share. W. later purchased 150 shares at 4½ on May 13, 1969 and 400 shares at 4½ on August 14, 1939.

Mr. S. testified that in January 1969 Dawson called him about DCA which he said was a very good company and that it was having a public offering at approximately $9 per share but that the stock would double within a year because the company looked exceptionally good. Dawson also told S. that whatever he purchased in the public offering he was expected to buy a large amount in the after market. On January 21, 1969 S. purchased 100 shares of DCA in the offering at 9½ and on January 22, 1969 he purchased 150 shares of DCA at 15.

Mr. F. testified that in 1969 he dealt with Dawson and Reno at Newport. He talked to Dawson because Reno was not in the office at the time and Dawson told him that Hill Bros. had a stock which could go to the $20 or better range. F. purchased 300 shares of Hill Bros. in the offering of May 12, 1969. Dawson told F. that Hill Bros. had something to

do with food in Miami, Florida but did not discuss the financial condition or earnings of the company.

Dawson told F. that Aero Systems was a $100 stock and that F. should buy it and put it in a safe deposit box and he would be a rich young man. F purchased 180 shares of Aero Systems on February 26, 1969 at 30 3/4. Dawson did not tell him anything about the earnings or financial condition of the company. Later when F. called Dawson to sell his Aero Systems stock Dawson said that Newport was trying to hold everybody in the stock so that there wouldn't be any panic selling. Dawson stated "wait, don't sell it, it is bottoming out, it is going to come back." F. testified that on approximately twelve occasions he attempted unsuccessfully to sell his Aero Systems stock to Newport.

F. testified that in March 1969 he attempted to sell some Micro Tenna stock to Newport and that he went to the Newport offices where he talked to Dawson who tried to talk him out of it by saying "it going up; you are making a big mistake; and it's going to be a big stock". However, F. testified, that when he insisted on selling the stock that Dawson finally went into a back room and came out with a check which he angrily threw at him.

F. testified that he had dealt with Reno at Robert Scott and had then followed Reno to Newport. He testified that he realized that some of the securities he was buying were speculative and that he might lose on his investment, but that he felt he would be able to sell out and take his losses. However, he was upset with Newport because he stated "I had a terrible time trying to sell anything up there".

Rex R. Reno

Reno was a security salesman at Newport from February 1969 until October 1969. He had previously been a salesman at Robert Scott and when he came to Newport he brought some of his customers with him. Five investor witnesses testified that Reno was the representative with whom they dealt at Newport and that he discussed or recommended to them at least eight of the stocks named in the order and that they made purchases of many of them based on his recommendations.

Mr. K. testified that in March 1969 Reno told him about Audio Visual International Corporation ("AVI"). Reno told him that it was a very exciting company and was coming out with a visual aid for teaching that would be sold to schools and would be a great success. Reno stated that the price of the AVI stock would go to $40 by Christmas. Reno did not discuss the earnings or financial condition of the company. As a matter of fact AVI had no operations and was still involved in research and development as at the end of January 1969. AVI was a spin off from International Book with one share of AVI being given to shareholders for every 20 shares of International Book owned on March 5, 1969.

On the basis of Reno's recommendations K. purchased 500 shares of AVI on March 18, 1969 at $30. On March 17, 1969 Reno sold to Newport 100 shares of AVI from his own account. This was not disclosed to K.

K. testified that Reno recommended Micro Tenna saying that it had bought a patent for a new short antenna that would

replace existing large antennas. Reno did not discuss the earnings or financial condition of the company and K. did not receive any written information on Micro Tenna prior to purchasing the stock. Based on Reno's recommendation K. purchased 400 shares of Micro Tenna on March 21, 1969. On March 17, 1969 Reno had sold to Newport 1500 shares of Micro Tenna from his own account. This was not disclosed to K. K. testified that he was never able to sell the AVI or Micro Tenna stock through Reno at Newport. Whenever he would attempt to do so, Reno would discourage him from selling by saying that the price of the stocks would go higher.

Mr. L. Testified that early in 1969 Reno told him about Shell's City which would be coming out at about $9 a share and that the stock would go to $18 or $20 a share. Reno told L. that the only way he could get shares in the offering was if he bought some in the after market. On April 17, 1969, L. purchased 100 shares of Shell City at 10½ in the offering and on April 18, 1969, he purchased 100 shares at 15 in the after-market.

L. testified that at the same time that Reno told him about Shell's City he also discussed the offering of Hill Bros. L. testified that Reno told him the same thing that he had in Shell's City that in order to buy Hill Bros. in the offering he would have to purchase some on the aftermarket. On the same day, May 12, 1969, L. purchased 100 shares of Hill Bros. in the offering at $2 and 100 shares in the aftermarket at $4.

Mr. S. testified that Reno recommended Shell's City to him and told him that he should contact his friends and get them to purchase the

stock also. Reno told S. that the most he could get in the offering was 300 shares and he suggested that S. buy some on the after market because the prospects for the stock were extremely good and the stock would go to $18 or $19 very rapidly. On Reno's recommendation S. ordered 300 shares of Shell City in the offering and 200 shares in the after market at the same time. S. was not told anything about the risk involved in purchasing Shell's City or the financial condition of the company, nor did he receive any literature from Newport prior to his purchase.

S. testified that in July 1969, he gave Reno a firm order to sell 1900 shares of International Book which he owned because the price had dropped from $17 to $12 a share. Reno tried to talk S. out of selling it, but when S. persisted Reno said he would sell the stock and call S. back. However, Reno did not sell the stock but convinced S. not to sell it. S. testified that Reno had originally suggested the International Book stock to him and had told him at one point in 1969 that it would be $50 by Christmas 1969 and reach $100 during the following year.

Mrs. H. testified that in 1969 she was secretary pro-tem of the Wall Street Investment Club ("Club") and that she took the minutes of a special meeting on April 17, 1969, at which Reno was the guest speaker. Reno recommended that the Club should buy Hill Bros. in the offering at $2 and he predicted that it would be selling at $14 or $15 by the end of 1969. Based on Reno's recommendation the Club voted to purchase Hill Bros. stock and H. personally purchased 100 shares of Hill Brothers in the offering at $2 a share. At the same meeting Reno stated that

Aero Systems would double in 1969 and that Micro Tenna and Hydro Tech spin-offs would be very big.

Mrs. McL. who was also a member of the Wall Street Investment Club testified that in May 1969 Reno told her about the offering of Hill Bros. and that the stock would probably triple. Based on this and Reno's discussion of Hill Bros. at the Club meeting previously referred to Mrs. McL. purchased 250 shares of Hill Bros. in the offering at $2 a share on May 12, 1969 and 250 shares in the aftermarket on May 14, 1969 at 4¼.

Stuart W. Fine

Seven investor witnesses testified concerning purchases of stocks named in the order through Fine who was a representative at Newport. Five of these witnesses testified concerning the purchases of Shell's City and among some of the things Fine told to various of these investors were that Shell's City would come out at 10½ and move rapidly upward, that the price would go to $27 or $30 within a month, and in order to buy stocks in the offering it would be necessary to buy some in the after-market as well, that purchasing shares in the aftermarket would improve chances for consideration for other new issues coming out in the future, such as Hill Bros., and that a good profit could still be made in the after-market as Newport needed to establish a trading pattern in the new shares and that it was very desirable to keep the market moving by purchasing additional shares in the after-market. Many of the investors did not receive a prospectus in advance of their purchases and relied solely on Fine's description of the company's activities concerning earnings, future prospects, and previous performance.

Two investor witnesses testified concerning the purchase of DCA shares through Fine. One of them testified that Fine told him DCA was coming out at 9½, would be 15 in about 3 weeks and 25 in about 6 months and that when he asked to buy 200 shares he was told that he would have buy 400 shares of American Foods in order to get 200 shares of DCA in the offering otherwise he could only get 100 shares of DCA in the offering. The other investor testified that Fine stated that

DCA was a hot issue and she would double her money but in order to buy any shares in the offering she would also have to buy some in the after-market.

In addition to the investor previously mentioned who testified concerning the tie-in purchase of American Food when he wanted to buy DCA, another investor testified that Fine told him that he should buy American Food stock in order to open an account at Newport and be eligible for new issues. Fine also predicted that the price of American Food would go to $12 or $14 a share.

Another investor testified that Fine recommended Micro Tenna stating among other things that it had a new antenna that was smaller than the current one in use, that within six months it would go from 18½ to $30 a share, and that within a year there would be a stock split. These representations concerning Micro Tenna were false and misleading as Micro Tenna had been spun-off from Aero Systems in late 1968, had no operations, never earned any money, and its sole business was research and development.

Two investor witnesses testified concerning purchases of Instrument Tech from Fine; one of them stated that he was told, among other things, that Instrument Tech had estimated earnings for 1969 of 70¢ per share and a million and a half backlog in orders. These representations were false and misleading and failed to disclose the true facts concerning Instrument Tech. See page 47 _supra_. Another witness testified that in 1969 he received a confirmation

in the mail from Newport showing that he had purchased 50 shares of Instrument Tech. He had never ordered the stock nor had he discussed buying it with Fine. However, Fine told him that Instrument Tech had new products coming out in the aircraft field and that there was going to be a merger which would make the price of the stock go up to $15 a share. When the investor expressed concern because he did not have the money to pay for the stock Fine told him not to worry, that he would sell other stock which the investor held at Newport so that the purchase wouldn't cost him any money. About a week later Fine called the investor and told him he should buy more shares since the merger still looked good and the price of the stock would go to 15. Based on this recommendation the investor purchased an additional 250 shares of Instrument Tech at 8¼. In January 1970 when the price of Instrument Tech was dropping the investor went down to Newport to see Fine and told him that he couldn't afford to take a serious loss with his limited funds. Fine told him that the price of the stock would come back after the stockholders meeting and merger. Fine urged him to purchase more shares of Instrument Tech which he did at 6 3/4.

Another investor testified that Fine told him about AVI and compared it with another stock which had come out at approximately $6 a share and gone to 45 and then split 5 for 1. Fine indicated that he expected AVI to have a similar performance. He also stated that AVI would earn $600,000 before taxes. The investor purchased 100 shares of AVI at $30 a share. The representations made by Fine concerning AVI had no basis in fact. See page 56 *supra*.

Glen E. Clymore

Five investor witnesses testified concerning purchasing 5 of the stocks named in the order from Clymore. Each of these investors testified concerning the purchase of Shell's City from Clymore and were told variously, among other things, that the earnings of Shell's City would go to $1.00 a share, that the stock would go to $20.00 a share within a short period of time, that information regarding a merger involving Shell's City would be released in the Miami Herald and possibly the Wall Street Journal, and that the price of the stock would go up as a result of that news, and that in order to purchase Shell's City in the offering they would have to buy shares in the aftermarket.

Clymore told one investor that American Foods had expanded its markets in Europe, that it would have a "lock" on the European markets in regards to the products it was exporting, and that he had talked to officers of the company and they had told him that the profits of the company were going to increase dramatically. Based on these recommendations the investor purchased 400 shares of American Foods.

Another investor, who also testified concerning Shell's City, stated that Clymore recommended Hill Bros. to him without giving any information concerning the financial conditional or earnings of the company. The investor purchased 100 shares of Hill Bros. in the offering and 2 or 3 days after the purchase asked Clymore to sell it but Clymore urged the investor not to sell telling him that the stock would go to $5 or higher. Clymore told the same investor

that Hydro Tech would increase from 3½ to $6 a share and relying on this recommendation the investor purchased 100 shares. Clymore did not tell him anything about the earnings or the financial condition of the company or the risks involved in buying Hydro Tech.

Hydro Tech Service Corporation, a New York corporation was acquired by Aero Systems in April 1968. In August 1968 a Florida corporation of the same name was organized as a subsidiary of Aero Systems and Aero Systems then sold its holdings in the New York corporation to the Florida corporation and the name was changed to Hydro Tech Corporation. In December 1968 Aero Systems distributed one share of Hydro Tech for two shares of Aero Systems. Hydro Tech was to engage in oceanography, including underwater electronics, sonar servicing and sales of parts. From its inception in December 1968 to early 1971 Hydro Tech was never profitable.

Another investor who had purchased Shell's City upon Clymore's recommendation testified that in January Clymore recommended DCA stock telling him that it would go higher and that there was a lot of buying pressure. The investor asked Clymore to purchase 100 shares of DCA in the offering and Clymore purchased 50 shares in the offering at 9½ on January 21, 1969 and 100 in the aftermarket at 15 on January 22, 1969. The investor testified that he had, in fact, never ordered any DCA stock in the aftermarket.

In their brief respondents take issue with several lists contained in the Division's brief "of alleged misrepresentations, omissions and the like which assertedly catalogue the specific alleged misdoings of the persons involved", on the grounds that this is a "wholesale technique of proving guilt on a cumulative basis . . . and does not relate the alleged misrepresentation to the persons, companies and the appropriate time frame." In addition, respondents assert, the Division has failed to disclose the case-made standards of conduct for broker-dealers in an attempt to create a standard for respondents which will result in making anything said by them (in securities sales) whether or not true or justified, misleading.

Respondents state that they do not have the capacity to "unprove" every charge made and then proceed to attack the testimony of the investor witnesses as being faulty, hazy, revengeful or "affected by a lack of sophistication which either at the time of purchase, or 2½ years later, changes a proper statement into a misrepresentation."

Respondents contend further, that a complete due diligence file was maintained on every company in which Newport had an interest and that it was created from materials brought by Wolfson from Executive and from materials sent in by the companies. Accordingly, respondents point out, any dissemination of false information or suppression of information came from the companies themselves and there is nothing to show that respondents knew or should have known facts which made their representations untrue.

The catalogue cited by the Division and objected to by respondents is not an abstract list of misrepresentations and omissions but a compilation of statements made or not made, taken from the sworn testimony of investors. The substantiation of Section 10(b) and Rule 10b-5 violations is largely dependent upon the testimony of individual investors. In this proceeding 33 investors testified concerning 80 securities transactions and the numerous misrepresentations, omissions and price predictions made to them by respondents. This testimony, which has been set forth and discussed at some length herein, was supported by confirmations, notes, checks, and other memoranda retained by the investors and is worthy of belief.[19/]

The list of statements made by Newport salesmen, which may be extracted from the investors testimony, runs practically the full scale of misrepresentations and omissions previously catalogued by the Commission as being fraudulent and misleading as may be seen from the following examples and citations.

The Commission has repeatedly held that predictions of specific and substantial increases in price of a speculative and unseasoned security are inherently fraudulent and cannot be justified. See, *e.g.*, *Armstrong, Jones and Company*, Securities Exchange Act Release No. 8420 p. 9 (October 3, 1968), *aff'd* 421 F.2d 349 (6th Cir. 1970), *cert denied*, 398 U.S. 958 (1970); *R.Baruch and Company* Securities Exchange Act Release No. 7932 p. 6 (August 9, 1966); *Richard J. Buck & Co.*, Securities Exchange Act Release No. 8482 (December 31, 1968), *aff'd sub. nom. Hanly v. S.E.C.*, 415 F.2d 589 (2nd Cir. 1969).

19/ *Keith Richard Securities Corp.*, 39 S.E.C. 231, 236 (1959).

The Commission has also held that predictions of a sharp increase in earnings with respect to such a security without full disclosure of both the facts on which they were based and the attendant uncertainties are inherently misleading. Richard Bruce & Co., Securities Exchange Act Release No. 8303, p. 6 (April 30, 1968) Richard J. Buck & Co., supra, at p. 8. It is irrelevant (1) that such predictions were couched in terms of opinion and the customer was advised that the security was speculative James DeMammos, Securities Exchange Act Release No. 8090, p. 3 (June 2, 1967), aff'd from the bench C.A. 2, Docket No. 31469 (October 13, 1967); R. Baruch and Company supra; (2) that the prediction was not expressed in terms of a guarantee James De Mammos, supra; (3) that the purchaser was a friend or former customer of the salesmen or initiated the transaction Armstrong, Jones and Company, supra; (4) that the customer was experienced or wished to speculate R. Baruch and Company, supra; (5) whether or not the customer relied on such representations Richard N. Cea Securities Exchange Act Release No. 9662 p. 6 (August 6, 1969); (6) whether or not the registrant's salesmen engaged in boiler room or high pressure tactics Armstrong, Jones and Company, supra; or (7) whether or not other types of fraudulent representations were made. See Arnold Securities Corp., Securities Exchange Act Release No. 7813 p. 3 (February 7, 1966).

Further, a salesman cannot recommend a security unless there is an adequate and reasonable basis for such a recommendation, Hanly v. S.E.C., supra, at p. 597. It is a fraud to make optimistic

representations or recommendations without the disclosure of known or reasonably ascertainable adverse information which would render them materially misleading Richard J. Buck & Co., supra, at p. 7; M.N. Gray Investments, Inc., Securities Exchange Act Release No. 9180, p. 4 (May 20, 1971); Alexander Reid & Co., Inc., 41 S.E.C. 372, 375 (1963). See Aviation Investors of America, Inc., 41 S.E.C. 566, 570 (1963) where the Commission stated:

> "A salesman who expressed an opinion about future market prices . . . impliedly represents that he has an adequate basis for such opinion. Absent such basis he violated his duty to deal fairly with customers and his implied representation is fraudulent."

Upon review of the record and consideration of all of the circumstances, as discussed herein, it is found that Newport, Wolfson, Susson, Dawson, Reno, Fine and Clymore, singly and in concert, willfully violated and willfully aided and abetted violations of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, as alleged in the order for proceedings.

Failure to Supervise

The Order for Proceedings alleges that during the relevant periods previously indicated herein Newport, Wolfson, Susson and Dawson failed reasonably to supervise persons subject to their supervision with a view to preventing the violations found herein.[20]

Wolfson, Susson and Dawson had supervisory responsibilities over the activities of registered representatives at Newport in 1969. Neither Wolfson nor Susson had any prior supervisory experience in the brokerage business. Wolfson and Dawson had more experience than Susson and they did most of the supervision of the registered representatives. Dawson had previously had supervisory responsibilities before organizing Newport and Reno and Fine had been under his direct supervison for several years immediately preceding the opening of Newport. When Newport opened Dawson set up the companies' information files and helped out in the cage and cashier departments. He was in charge of the internal operations and executed all listed business. In March, 1969 Susson assumed supervision of Regulation T procedures and continued in that capacity in 1970 and 1971. Wolfson was responsible for checking all of the salesmen's transactions when he executed them as the principal trader. Wolfson also had the final say on all hiring at Newport. Therefore all of the

---

20/ Section 15(b)(5)(E) of the Exchange Act, as added by the 1964 amendments, provides an independent ground for the imposition of a sanction against a broker or dealer or a person associated with a broker or dealer who ". . . has failed reasonably to supervise, with a view to preventing violations of such statutes, rules and regulations, another person who commits such a violation, if such other person is subject to his supervision.

supervisory responsibility over the various phases of Newport's business was shared by Wolfson, Susson and Dawson.

When Newport opened for business at the end of 1968 there wasn't time to train registered representatives and accordingly, experienced salesmen were desired. Three former salesmen at Newport testified that there were no training sessions or seminars and no written information furnished to registered representatives concerning the proceduresthat should be followed in the sale of securities. No directions were furnished to registered representatives on how to sell securities and on one occasion when Wolfson was asked what to tell a customer, he said "just tell them it is going up".

Former representatives testified that there was no regular procedure at Newport for the dissemination of information concerning the companies whose stock they were selling and the representatives relied upon Wolfson, Susson, Dawson and Reno for information on the various companies. Due diligence files were maintained by Dawson but were kept locked for the first month Newport was in business and after that they were opened to the salesmen upon asking Dawson. Wolfson testified that there was a tendency for the files to get lost and out of shape. There was no written record kept of what went into the files nor was outdated material removed from the files.

Reno who was under Commission sanction at the time he became associated with Newport (see page 5 supra) was to be closely supervised by Wolfson or in his absence Susson. Reno and the other

registered representatives at Newport were to have all purchases and sales of securities approved by Wolfson and all execution of purchases or sales were likewise to be approved and executed by Wolfson. However, the record discloses that some 152 order tickets that Reno wrote in connection with purchases in the Hill Bros. offering were not time stamped, or signed by Wolfson, Susson or any other principal at Newport.

Respondents contend that they are entitled to rely on that portion of Section 15(b)(5)(E) which states that:

> "No person shall be deemed to have failed reasonably to supervise any person, if —
> (i) there have been established procedures, and a system for applying such procedures, which would reasonably be expected to prevent and detect, insofar as practicable, any such violation by such other person, and
> (ii) such person has reasonably discharged the duties and obligations incumbent upon him by reason of such procedures and system without reasonable cause to believe such procedures and systems were not being complied with."

Respondents urge that procedure and system existed at Newport but state that they cannot prove that they informed the representatives of the chain of supervision. They state that in a small office it must be assumed that the representatives had some inkling as to who was responsible for supervising.

However, respondents failed to support this assertion that supervisory procedures were in effect except by their own testimony. Respondents did introduce into evidence three memoranda on price predictions prepared by Newport's general counsel for distribution to employees. These were for the purpose of warning salesmen about

improper price predictions, or as Wolfson told another representative showing the difference between being "bullish" and making an improper prediction.

The record discloses that most of the supervision of the registered representatives was done by Wolfson and Dawson while Susson was responsible for the enforcement of Regulation T. Thus, all of the registered representatives employed at Newport including Reno, Fine and Clymore were under the supervision of the three principals.

The Commission has long held that principals of a security firm have a responsibility to exercise adequate supervision of the firm's activities so as to prevent violations of the Securities laws.[21/] A contrary rule "would encourage ethical irresponsibility by those who should be primarily responsible."[22/]

On the basis of the findings previously made herein that Reno, Fine and Clymore committed violations of the federal securities laws as charged in the Order for Proceedings, it is found that Wolfson, Susson and Dawson failed to properly discharge their supervisory responsibilities in order to prevent such violations.

21/ Midland Securities Corp., 40 S.E.C. 635 at p. 639-40 (1958); Webb Securities, Inc., 38 S.E.C. 594, 597-98 (1958); Bond and Goodwin, Inc., 15 S.E.C. 584, 601 (1944); General Investing Corporation, 41 S.E.C. 952, 958 (1964).

22/ R. H. Johnson & Company v. S.E.C., 198 F.2d 690, 696-97 (2nd Cir. 1952); cert. denied 344 U.S. 855 (1952).

OTHER MATTERS

Respondents argue that they have been denied due process and a fair hearing by virtue of the rulings in connection with their efforts to obtain discovery before the hearing, and by rulings in connection with their cross-examination of witnesses during the course of the hearing. The rulings concerning discovery were affirmed by the Commission, the other rulings were not appealed.

Upon consideration of the present arguments it does not appear that the rulings heretofore made should be disturbed.

PUBLIC INTEREST

Respondents urge that the sanctions requested by the Division that Newport's registration as a broker-dealer be revoked and that Wolfson, Susson and Dawson be barred from association with any broker-dealer is too harsh in light of the circumstances which have been disclosed in this case. In this connection respondents call attention to Commission Order of May 23, 1972 (Sec. Exch. Act Rel. No. 9614) imposing remedial sanctions on Executive Securities. Respondents suggest that the present proceeding against them was brought because of possible irregularities involving the offer and sale of some of the same stocks [23/] involved in the Executive matter and submit that if any improprieties occurred in connection with those stocks they were the fault of the companies or individuals

---

23/ Hill Bros. Shell's City and DCA were all hot issues underwritten by Executive. (See pp. 6-11, *supra*)

associated with the companies and Executive and not respondents. (See, also, p. 65 *supra*).

Further, respondents point out that there have been no customer complaints to the NASD or the Commission and no civil suit has been filed in connection with any transaction effected by Newport.

Respondents willful [24/] violations of the Securities Act and Exchange Act require the application of sanctions which cannot be evaded by attempting to shift responsibility for their conduct to others. While the record does not reflect prior violations on the part of Newport, Wolfson, Susson and Dawson it does substantiate the findings herein.

The nature and extent of the violations found herein and the fact that they were committed by principals of a registered broker-dealer demonstrates a contempt and disregard for the federal securities laws which cannot be overlooked when considering appropriate sanctions. Respondents operated in an unscrupulous manner in a relatively affluent community where many elderly retired persons on fixed incomes were inviting prey to their seductive salesmanship.

The activities engaged in by respondents are perhaps best described in *MacRobbins & Co., Inc.*, 41 S.E.C. 116, at 119, 120, where the Commission said:

> "Commonly characterized as 'boiler-room' procedures, they involve a concerted, high-pressure effort -- typically by

---

24/ It is well established that a finding of wilfulness under Section 15(b) of the Exchange Act does not require an intent to violate the law and that it is sufficient that a respondent intentionally engaged in conduct which constituted a violation. *Tager v. Securities and Exchange Commission*, 344 F.2d 5, 8 (C.A. 2, 1965); *Dunhill Securities Corporation*, Sec. Exch. Act Rel. 9066, p. 4 (Jan. 26, 1971).

> telephone -- to sell a large volume of one or several promotional or speculative low-priced securities to unknown persons without any concern for the suitability of such securities in the light of the customers' investment needs or objectives and by the use of false and deceptive means. The sales techniques used are by their very nature not conducive to an unhurried, informed and careful consideration of the investment factors applicable to the securities involved.. . . These boiler-room operations, relying for the most part on oral representation, subject the requirements of fair dealing to their greatest test and the enforcement of the statutory prohibitions against fraud to grave difficulties."

In view of all of the circumstances it is concluded that the number and character of the violations is such that the public interest requires revocation of Newport's registration as a broker-dealer. With respect to respondents Wolfson, Susson and Dawson it is concluded that the public interest requires that each of them be barred from being associated with a broker-dealer.[25]

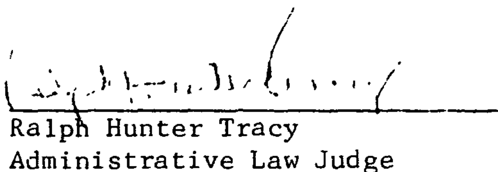
ORDER

Accordingly, IT IS ORDERED that the registration as a broker-dealer of Newport Securities Corp. is revoked and the company is expelled from membership in the National Association of Securities Dealers, Inc.; and that A. Gurdon Wolfson, Martin Susson and Roy O. Dawson, and each of them, is barred from association with a broker-dealer.

25/ It should be noted that a bar order does not preclude the person barred from making such application to the Commission in the future as may be warranted by the then-existing facts. Fink v. SEC, (C.A. 2, 1969), 417 F.2d 1058, 1060; Vanasco v. SEC, (C.A. 2d, 1968) 395 F.2d 349, 353.

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

Pursuant to Rule 17(f), this initial decision shall become the final decision of the Commission as to each party who has not within fifteen days after service of this initial decision upon him, filed a petition for review of this initial decision pursuant to Rule 17(f), unless the Commission, pursuant to Rule 17(c) determines on its own initiatve to review this initial decision as to him. If a party timely files a petition for review, or the Commission takes action to review as to a party, the initial decision shall not become final with respect to that party. 26/



Ralph Hunter Tracy
Administrative Law Judge

February 16, 1973
Washington, D.C.

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