INITIAL DECISION RELEASE NO. 66

ADMINISTRATIVE PROCEEDING
FILE NO. 3-8206

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of	)	INITIAL DECISION
	)	JUNE 27, 1995
Paul C. Kettler	)	

Appearances: Jerrold H. Kohn, Esq.
Jonathan H. Stein, Esq.
Attorneys for the Division of Enforcement
Securities and Exchange Commission

Dennis A. Delman, Esq.
Attorney for Respondent

Before: Glenn Robert Lawrence
Administrative Law Judge

These public proceedings were instituted by order of the Commission dated October 26, 1993 pursuant to Section 15(b) and 19(h) of the Securities Exchange of 1934 to determine whether allegations of misconduct made by the Division are true and what, if any remedial action would be appropriate in the public interest. In substance, The Division alleges that Respondent, Paul C. Kettler (Respondent) failed reasonably to supervise Randal C. Forman (Forman) with a view towards preventing his violations of the federal securities laws, within the meaning of Sections 15(b)(4)(E) of the Securities Exchange Act of 1934 (Exchange Act), in connection with initial public offering (IPO) and trades in shares and warrants of Windy City Capital Corporation.

Respondent, by answer received in this office November 22, 1993, in substance, denied the allegations relating to the violation of the securities laws and failure to supervise. He admitted ownership of Kettler & Company and the non-controversial facts relating to the IPO.

The findings and conclusions herein are based upon the preponderance of the evidence as determined by the record and upon my observation of the various witnesses that testified at the hearing that was held in Chicago, Illinois, February 21, 1995, as well as the briefs, proposals of facts and law and the argument of the parties.

FINDINGS OF FACT 1/

The Respondent, a resident of Chicago, Illinois, became registered as a broker-dealer in 1982 and began operating as Kettler & Company (Kettler & Co.), the main office of which was located in Chicago, Illinois (Chicago Office).2/ (Division's Exhibit 22 - Stipulations, ¶ 2)3/

At all relevant times: Respondent was registered with the National Association of Securities Dealers (NASD). (Stip. ¶ 3) Kettler & Co. was a sole proprietorship, of which Respondent was the sole proprietor. (Stip. ¶ 5) Respondent was the designated compliance officer of Kettler & Co. (Div. Ex. 23A, p. 30; Stip. ¶ 8).

Respondent has been sanctioned on four occasions by the NASD. Two of these actions were appealed to, and sustained by, the Securities and Exchange Commission

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1/ Respondent, on June 1, 1995, filed a "Response to Proposed Findings of Fact and Conclusions of Law of Division of Enforcement" with a purported affidavit attached thereto. Inasmuch as Respondent failed to offer into evidence any proofs at the hearing, any documents he has submitted to this Office, by way of affidavits or otherwise, are considered solely in the nature of argument and are not in evidence. It is therefore not possible to credit facts claims the Respondent has made in his submission. Further, Respondent's disinclination to appear and testify in his own behalf creates a negative inference that had he testified it would be adverse to his interests. Additionally, I agree with the Division that the "affidavit" filed by Respondent is defective in that it is not signed before a notary public.

2/ The respondent admits this allegation but further alleges that he voluntarily withdrew his broker-dealer license on November 23, 1990 and the Commission accepted the withdrawal. This is in support of an argument that has been raised and already determined by the Commission by its order on March 13, 1995. The Commission at that time rejected Respondent's argument that his firm's withdrawal is tantamount to a release from liability of the Respondent individually. This issue will be discussed further in the conclusion section.

3/ "Division's Exhibit" will hereinafter be referred to as "Div. Ex." "Stipulations," which are marked as Div. Ex. 22, will hereinafter be referred to as "Stip."

(Commission). These actions are as follows:

1. In the Matter of Paul C. Kettler, SEA Release No. 31353, 52 SEC Docket 3243 (October 26, 1992) (Commission sustained NASD sanction of censure, $10,000 fine, 30 day suspension and requirement of requalification as a general securities principal against Respondent, based on his permitting the association with his firm of an individual who had been barred by the NASD);
2. In the Matter of Paul C. Kettler, SEA Release No. 31354, 52 SEC Docket 3249 (October 26, 1992) (Commission sustained NASD sanction of censure and a $5,000 fine against Respondent, based upon his failure to supervise adequately a salesman who engaged in unsuitable options trading);
3. In the Matter of Kettler & Company, et. al., No. ATL-1037 (December 8, 1989) (By consent, NASD censured and fined Respondent $7,500, settling an NASD complaint alleging that Kettler & Co., acting through Forman, charged unfair prices in over-the-counter principal transactions); and
4. In the Matter of Kettler & Company, et. al., No. ATL-1056 (December 8, 1989) (By consent, NASD censured and fined Respondent $10,000, settling an NASD complaint alleging that he failed to supervise Forman, who allegedly effected principal transactions in contravention of the NASD's anti-manipulation rule and markup policy).4/

From in or about October 1987 through at least August 1988, Kettler & Co. operated

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4/ This Office has previously taken Official Notice of these matters.

approximately 15 branch offices, including a branch office located in or near Ft. Lauderdale, Florida (Florida Branch). (Stip. ¶ 4).

At all relevant times, Respondent owned the Florida Branch. (Stip. ¶ 6).Respondent admits this allegation and further alleges that the Florida Branch operated as an office of supervisory jurisdiction.

At all relevant times, the branch manager of the Florida Branch was Forman. (Stip. ¶ 7). In that position he was responsible for, among other things: (1) supervising the registered representatives in the office; (2) supervising sales; (3) making markets in securities and supervising market-making activities; and (4) determining bid and ask prices for securities traded in the Florida Branch.5/ (Transcript of Proceedings pp. 110-111, 124).6/

At all relevant times, Respondent was responsible for supervising Forman in connection with the sales and market-making activities of the Florida Branch, and was ultimately responsible for the overall supervision of the Florida Branch. No one else supervised Forman. (Stip. ¶ 9; Tr. p. 110; Div. Exs. 23A, p. 30; 23E, p. 254; 25, ¶ 56; and 26, ¶ 22).

During the period October 1987 through June 1989, Forman was the head trader, and, in fact, the only trader, for Kettler & Co. No one else was ever a trader for Kettler & Co. during that period. As part of his responsibilities as head trader, Forman set prices for purchases and sales of securities traded by the Florida Branch. (Tr. pp. 123-24). On or

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5/ Respondent admits this allegation but also alleges that Forman was independent and could make decisions on his own without the respondent's consent.

6/ "Transcript of Proceedings" will hereinafter be referred to as "Tr."

about October 13, 1987, Windy City Capital Corporation (Windy City) filed a Form S-18 Registration Statement with the Commission for an initial public offering (IPO). The Registration Statement became effective on or about February 10, 1988. (Stip. ¶ 14). Kettler & Co. was the sole underwriter for the Windy City IPO. (Stip. ¶ 13).

The terms of the Windy City IPO were as follows:

1. The IPO was effective on February 10, 1988. (Stip. ¶ 14).
2. The IPO consisted of 2,000 units at an offering price of $100 per unit. (Stip. ¶ 14). This offering price was a completely arbitrary amount. (Div. Ex. 23E, p. 304).
3. Each unit consisted of 2,000 shares of Windy City common stock and 9,000 redeemable warrants. (Stip. ¶ 14).
4. The closing date of the offering was July 9, 1988. (Stip. ¶ 14).
5. The offering was on a "best efforts, all-or-none" basis, which meant that, for the offering to be successfully completed, all of the units had to be sold by the close of the offering. (Stip. ¶ 14).

Kettler & Co. began selling units of Windy City to its customers in the beginning of July 1988. All of the units were sold within approximately two weeks. (Tr. p. 136). All 2,000 units were sold by Kettler & Co. to its customers by the July 9, 1988 closing date. All of these units were sold by registered representatives in the Florida Branch. (Stip. ¶ 15) Respondent was in contact with Forman during the period that the units of Windy City were being sold. Forman kept Respondent informed as to how many units had been sold and how many more units needed to be sold to successfully complete the IPO. (Tr. pp. 136-137; Div.

Ex. 25, ¶ 41).

After the conclusion of the Windy City IPO, and prior to the beginning of secondary market trading in Windy City common stock, Forman adopted a strategy in which Kettler & Co. would purchase all the units of Windy City and sell Windy City common stock to its retail customers. Respondent and Forman agreed to this strategy prior to its implementation. (Tr. pp. 138-39). During the period July 18 through July 29, 1988, Kettler & Co. acquired 3,406,525 shares of Windy City common stock. Of this amount, 3,214,000 shares were acquired by Kettler & Co.'s purchase of 1,607 units of Windy City from its customers in the Windy City IPO. The 3,214,000 shares represented 80 percent of the outstanding shares. (Div. Exs. 1-3; Tr. pp. 62-63).7/

Kettler & Co. purchased 1,597 of the 1,607 units described in Paragraph 18 above for $200 per unit, or $.10 per share, and the other ten units for $150, or $.075 per share. (Div. Exs. 1-3; Tr. pp. 56-57). Forman, as the head trader for Kettler & Co., determined these prices.8/ (Tr. p. 139).

From no later than July 14, 1988 through at least July 29, 1988, Kettler & Co. listed its name as a market maker of Windy City securities in the National Bureau of Quotations Pink Sheets (Pink Sheets). However, during that time, Kettler & Co. never entered bid or ask prices into the Pink Sheets. (Div. Ex. 6; Tr. pp. 52-53). During that period, the only

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7/ Respondent obviously knew that his company controlled Windy City, vice Respondent's contention that the market was competitive.

8/ This figure, which assumes the value of the warrants is zero, gives the highest possible contemporaneous cost to the common stock. Assigning a value to the warrants would cause the contemporaneous cost to be lower, resulting in even higher markups than those proven by the Division.

other broker-dealers that were listed in the Pink Sheets were Wien Securities Corp. (Wien) and Greentree Securities Corp. (Greentree). However, during that time, neither Wien nor Greentree entered bid or ask prices in the Pink Sheets or executed any retail transactions in Windy City securities. (Div. Ex. 6; Tr. pp. 52-53).9/ On July 19, 1988, Kettler & Co. began selling Windy City common stock to its customers. (Tr. pp. 137-138; Div. Exs. 2-3).

Forman was responsible for making markets in the common stock and units of Windy City. The prices at which the shares of common stock were bought from and sold to the public were determined solely by Forman. (Tr. p. 140). During the period July 19 through July 29, 1988, Kettler & Co. sold 3,374,800 shares of Windy City common stock to its customers at prices beginning at $.16 per share and increasing during the period to as high as $.26 per share. (Div. Ex. 1; Tr. pp. 62-63). At least 90 percent of these sales were solicited transactions. (Tr. pp. 111, 170-171).

During the period July 19 through July 29, 1988, Kettler & Co., through Forman, executed 449 transactions in which the 3,374,800 shares of Windy City common stock were sold to its customers. A total of 406 of these trades, or 90 percent, were executed at markups that were at least ten percent above the prevailing market price of Windy City common stock. A total of 318 of those trades were executed at markups in excess of 100 percent over the prevailing market price. (Div. Exs. 1-3, 7; Tr. p. 64-66). Respondent's

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9/ The Respondent disclaims knowledge of whether Wien or Greentree were executing retail transactions and he alleges that he believed that Windy City was being traded in a competitive market. These claims are not considered credible in light of the history of trades by Kettler & Co. during the critical period and the close contact between Forman and Kettler. As discussed supra, Respondent's argument, by implication, that Wien and Greentree created a competitive market is without support.

claim that he thought Windy City trades were competitive is not credible.

During the period July 19 through July 29, 1988, Kettler & Co. was the only broker-dealer who executed retail transactions in any Windy City securities, including common stock. (Div. Exs. 1-6; Tr. pp. 51-53, 145). Respondent's disclaimer of knowledge is not credible.

During the period July 18 through July 29, 1988, there were only four wholesale transactions in Windy City securities, two each between Kettler & Co. and Wien and Kettler & Co. and Greentree, respectively. (Div. Exs. 1-6; Tr. pp. 51-53, 145). The registered representatives at Kettler & Co did not disclose to the customers who purchased Windy City common stock the amount of the markup that those customers were charged, nor, in fact, did they ever disclose to those customers that they were being charged any markup at all. (Tr. pp. 150-152, 175).

None of the registered representatives at Kettler & Co. were instructed to disclose to the customers who purchased Windy City common stock the amount of the markup that those customers were charged, or that they were being charged any markup at all. (Tr. pp. 150-152, 175). Respondent admits this finding but argues that the representatives had no duty of disclosure. Out of fairness and under the "shingle theory", the representatives should have advised customers of exorbitant markups. Charles Hughes & Co. v. SEC, 139 F.2d 434 (2d Cir. 1943), cert. denied 321 U.S. 786 (1943).

During the period July 19 through July 29, 1988, virtually all of the common stock of Windy City was owned either by Kettler & Co. or customers of Kettler & Co. (Div. Exs. 1-6; Tr. p. 113). As a result, Kettler & Co. was able to exercise control over the supply of

Windy City common stock. (Tr. pp. 113-114). Respondent denies this finding but does not offer any proof to support his denial.

During the period July 19 through July 29, 1988, Kettler & Co. was the seller in 100 percent of the retail transactions in Windy City common stock, and was a party to 100 percent of the wholesale transactions in that stock. (Div. Exs. 2, 4-6). The Respondent admits the allegation but disclaims knowledge as to whether Wien or Greentree were executing trades.

During the period July 19 through July 29, 1988, the prices at which Windy City common stock was sold to customers bore no relationship to prices in a free, open and competitive market. This fact was evidenced by the following:

1. Forman arbitrarily increased the price of Windy City common stock for several reasons, including: (a) to create a history of successful underwritings; (b) so that customers could make a profit on their purchase of Windy City securities; and (c) to attract registered representatives from other broker-dealers to work at Kettler & Co. (Tr. pp. 143-144);
2. There were no news announcements regarding Windy City (Tr. p. 147);
3. While the price at which Windy City common stock was sold to retail customers increased, Kettler & Co. continued to purchase the stock from customers at nearly constant prices. Of the 3,406,525 shares of Windy City common stock reacquired by Kettler & Co. in the secondary market, 3,214,000 shares, or 94 percent, were acquired at $.10 per share (Div. Exs. 1-3; Tr. 62, 63);

4. Forman controlled the bid and the ask prices by keeping the bid price low so that Kettler & Co. would not have to commit too much of its capital to purchase stock from customers (Tr. pp. 146-147); and

5. At least 90 percent of the demand for Windy City common stock was created by the sales force in the Florida Branch. (Div. Ex. 23E, p. 414; Tr. pp. 142-143, 146). Much of this demand resulted from the use of aggressive and misleading sales tactics. (Div. Ex. 26, ¶¶ 13-14; Tr. pp. 171-175).

Though Respondent denies these findings he offers no proof in support of his denial.

The registered representatives at Kettler & Co did not disclose to the customers who purchased Windy City common stock that Kettler & Co. had manipulated the price of the stock or that the price of the stock bore no relationship to a price in a free, open and competitive market. (Tr. p. 151, 178-179). Though Respondent denies these findings he offers no proof in support of his denial.

None of the registered representatives at Kettler & Co. were instructed to disclose to the customers who purchased Windy City common stock that Kettler & Co. manipulated the price of the stock or that the price of the stock bore no relationship to a price in a free, open and competitive market. (Tr. pp. 151-152, 178). Though Respondent denies these findings he offers no proof in support of his denial.

Registered representatives made false and misleading statements to customers and engaged in other fraudulent practices in order to induce them to purchase Windy City common stock. These included, among others, the following:

1. Assurances that the customer would earn a profit on their investment (Div. Ex.

26, ¶ 14; Tr. pp. 171-172);

2. Statements that the management of Windy City "have great expertise" when there was no basis for such statements (Tr. pp. 172-173); and

3. Leading customers to believe that important news about the company was being announced, in fact, there were no such announcements. (Tr. p. 147, 173).

Though Respondent neither denies or admits these findings, he contends that he did not have knowledge of the conduct of the registered representatives. His statement is not credible.

At all relevant times, Kettler & Co. had a Procedures Manual that set certain supervisory procedures for the Florida Branch. No supervisory procedures were in effect in the Florida Branch other than those set forth in the Procedures Manual. (Div. Exs. 9; 23C, pp. 12-13; and 25, ¶ 44; Tr. p. 116). Denying this finding, Respondent claims that the supervisory procedures were only provisional and not used. I don't find this statement credible.

The Procedures Manual was reviewed and approved by the Respondent in late 1987. (Div. Ex. 23C, pp. 22-23). I do not find Respondent's denial of this finding is supported. The Procedures Manual was revised on June 10, 1988 to include the following provisions, among others, governing markups by Kettler & Co.:

1. That the company would operate its mark-up/mark-down policy in accordance with Article III, Section 4, of the Rules of Fair Practice.10/ (Div. Ex. 9, p.

10/ During the hearing of this matter, this Office took official notice of the NASD manual that contain the rules governing broker-dealers (Tr. p. 20).

28; Stip. ¶ 11);

2. That the amount of the mark-up/mark-down would generally be disclosed to the customer, if practicable, in advance of the trade (Div. Ex. 9, p. 28; Stip. ¶ 11); and

3. That, at the end of each trading day, copies of the trade blotter containing activity in the trading account would be sent to the Chicago Office of Kettler & Co. (Div. Ex. 9, p. 27).

Respondent admits this finding but denies that the manual was implemented.

Respondent wrote, and approved the implementation of, the markup policies described above. (Div. Exs. 9 and 25, ¶ 45; Tr. p. 117). Respondent admits this finding but denies that the manual was implemented. Respondent devoted approximately 50 percent of his time at Kettler & Co. to the Florida Branch. (Div. Ex. 23E, p. 259).

In July 1988, the Florida Branch accounted for approximately 90 percent of the sales volume for Kettler & Co. and approximately 95 percent of the trades executed by Kettler & Co. (Div. Ex. 25, ¶ 12). Respondent denies this finding but does not provide support for his denial.

Respondent went to the Florida Branch on a regular basis, including 10-12 times in 1988. During some of these visits, he participated in sales meeting with registered representatives concerning Windy City. (Div. Ex. 23E, pp. 259, 317, 379).

Because of his regular visits to the Florida Branch, Respondent knew most of the registered representatives in the office. (Div. Ex. 23B, p. 94). When he was present in the Florida Branch, Respondent observed the sales floor operation and was present when

registered representatives were soliciting customer orders. (Tr. pp. 114-15). Respondent denies this finding but provides no support for his denial.

When he was not present in the Florida Branch, Respondent spoke to Forman virtually every day. (Div. Ex. 23E, p. 254; 26, ¶ 22). Respondent denies this finding but provides no support for his denial.

As early as January 8, 1988, Respondent was aware of NASD concerns about possible excessive markups in the Florida Branch. (Tr. p. 117-118). In June 1988, the NASD conducted an examination of the Florida Branch. This exam resulted in allegations by the NASD that there were significant violations of Article III, Section 4 of the NASD's Rules of Fair Practice. (Div. Ex. 20, p. 2). In the spring or summer of 1988, prior to the commencement of secondary market trading in Windy City, Respondent was informed by letter from the NASD, and on June 10, 1988, Respondent was informed in a meeting with the NASD, of the NASD's allegations. (Div. Exs. 20 and 25, ¶¶ 42-43). Respondent does not recall NASD raising concerns about the Florida office. However, as argued by the Division, Respondent has admitted that in January, 1988 NASD had expressed such concerns.

Respondent wrote and implemented Kettler & Co.'s markup policies described above as a result of the NASD's concern about possible excessive markups in the Florida Branch. (Div. Ex. 25, ¶ 45; Tr. pp. 117-118). Respondent admits the preparation of the manual but denies the balance of the finding. However, there is no support for the denial. The Division convincingly argues that the markup procedures, according to Respondent's stipulation, was implemented. (D. Ex. 9).

Even after implementing the written markup policy, Respondent never instructed Forman on how to adhere to that policy in the Florida Branch. (Tr. p. 119). Respondent denies this finding but provides no support.

During the period from at least January 1, 1988 through at least August 5, 1988, Ameritrade, Inc. (Ameritrade) was the exclusive clearing broker for Kettler & Co. All trades of securities executed by Kettler & Co. were thus processed through Ameritrade. (Div. Ex. 2, ¶ 3). Respondent denies this finding but provides no support for his denial.

During the period from at least January 1, 1988 through December 31, 1988, on a daily basis, Ameritrade prepared and sent to the Florida Branch, via telefax, reports known as the Settlement Computation Page and the House Account Report. (Div. Ex. 19, ¶ 3). Respondent admits this finding except denies that he saw the Computation page and House report on a daily basis.

During the period from at least July 1, 1988 through December 31, 1988, every Wednesday, Ameritrade sent to Kettler & Co.'s Chicago Office a complete set of the House Account Reports from the beginning of the month through and including the close of the prior business day. (Div. Ex. 19, ¶ 3).

The House Account Reports prepared by Ameritrade reflected all the activity in Kettler & Co.'s trading account, including the trade date, the settlement date, the amount of the transaction, the type of transaction, whether the transaction was a buy or a sell, the quantity, the name of the security and the price. (Div. Ex. 19, ¶ 2). Respondent denies this finding and avers that Ameritrade was the exclusive clearing broker only for the Florida branch.

During the months of June and July 1988, either Laura Ramu or Kathy Boyle, both of whom were employed in the Florida Branch, faxed, on a daily basis, the Ameritrade Settlement Computation Page and the Ameritrade House Account Report to the Chicago Office. (Div. Exs. 23C, p. 15 and 27, ¶ 6; Tr. pp. 127-131). Respondent denies the facts but does not provide support for his denial. In its Reply, the Division persuasively argues the investigative testimony (D. Ex. 23C, p. 14, lines 7-12) reflects that Respondent received five or six sheets daily.

Beginning in January or February 1988 and continuing until at least December 1989, Respondent arranged for the Florida Branch's daily trade blotter to be faxed to the Chicago office at the end of each trading day. (Div. Ex. 25, ¶¶ 1, 30). Respondent denies the facts but does not provide support for his denial.

The daily trade blotter contained detailed information about each trade that was executed by the Florida Branch on that day, including customer account name, whether the trade was a buy or a sell, price, quantity and the name of the security. (Div. Ex. 25 ¶ 31; Tr. pp. 120-122).

Every day in the Florida Branch, a retail quote sheet was distributed to the registered representatives. These sheets contained the bid and ask prices for securities in which Kettler & Co. was making a market, including Windy City units and common stock. The bid and ask prices were determined by Forman. These retail quote sheets were faxed to the Chicago Office every day during July 1988. (Div. Ex. 8; Tr. pp. 124-26). Respondent denies the facts but does not provide support for his denial.

Phillip K. Meegan (Meegan) was the operations manager in the Chicago Office. In

this position, he had no supervisory responsibilities over any registered persons at Kettler & Co., nor did he have supervisory responsibilities over any sales or market making activity in the Florida Branch or elsewhere. (Div. Exs. 23A, p. 25 and 25, ¶ 2).

When Respondent was not in the Chicago Office, he and Meegan frequently talked by telephone about that day's business, sometimes as often as two or three times per day. (Div. Ex. 25, ¶ 19). Respondent avers that he talked in excess of three times per day to Meegan.

In the course of the normal business of the Chicago Office, Respondent received, on a frequent and regular basis, telephone calls, faxes and mail. These faxes included, on a daily basis, numerous faxes from the Florida Branch. If Respondent was present in the Chicago Office, Meegan would put calls through to him, and hand him the faxes and his mail. (Div. Ex. 25, ¶¶ 20, 38). Respondent denies the allegations of this finding but provides no support.

Meegan's typical practice regarding telephone calls for Respondent, when Respondent was not in the Chicago Office, was to take a message and leave it on his desk. However, if the call was from the Florida Branch, and concerned an issue that required Respondent's immediate attention to resolve, Meegan followed one of three courses of conduct. First, he would direct the caller to call Respondent at home, if Meegan knew he was at home. Alternatively, Meegan would call Respondent at home and ask him to return the call. More often than not, during 1988, the caller from the Florida Branch was Forman. Finally, Meegan may have faxed to Respondent, at his home, a copy of the message given to Meegan by the caller. (Div. Ex. 25, ¶ 21).

Meegan's typical practice regarding faxes and mail for Respondent, when Respondent was not in the Chicago Office, was also to follow one of three courses of conduct. If the fax or mail required Respondent's immediate attention, Meegan would call him at home to discuss it with him. Alternatively, Meegan would place the fax or mail on his desk, for him to review that night or whenever he next came into the Chicago Office. At times, at Respondent's request, Meegan also faxed documents to him at home. (Div. Ex. ¶ 22).

Respondent installed a fax machine in his home, at Meegan's request, prior to June 1988, so that Meegan could fax information to him that required his review. (Div. Ex. 25, ¶ 23). On occasion, the Florida Branch personnel faxed information, including trading information, to the Respondent at his home. (Div. Ex. 25, ¶¶ 24-25).

When the trade blotter and other documents from the Florida Branch were received by fax in the Chicago Office, Meegan would give them to the Respondent, or, if he was not in the office, put them on his desk. (Div. Ex. 25, ¶¶ 33, 38).

Respondent reviewed each of the trade blotters on a daily basis, as well as all faxes he received from the Florida Branch. (Div. Exs. 23C, pp. 14-15, 18; 25, ¶¶ 34-35; and 26, ¶ 22). Respondent denies this finding but provides no support.

After the end of each month, Ameritrade sent to the Chicago Office a monthly trade run of activity in the Florida Branch. Meegan received this run and gave it to the Respondent. Respondent then spent several hours analyzing the information on the run. (Div. Ex. 25, ¶¶ 36-37 and Exhibit A attached thereto).

During the period July 19 through July 29, 1988, Respondent was aware that the price of Windy City common stock was increasing. (Div. Exs. 23E, pp. 435-36 and 25, ¶

35). Respondent admits this finding except states that he believed Windy City was being sold in a competitive market.

During the period July 19 through July 29, 1988, based on the reports he received, his conversations with Forman, and his visits to the Florida Branch, all of which is described above, Respondent had information available to him that showed that the Florida Branch: (1) purchased 80 percent of the outstanding common stock of Windy City from IPO purchasers; (2) in most cases, paid $.10 per share for the common stock; (3) sold the common stock to customers at rapidly increasing prices; (4) sold the common stock at excessive markups; (5) controlled the supply of Windy City securities and dominated and controlled the retail market in Windy City securities; and (6) manipulated the price of Windy City securities. (See, e.g., Div. Exs. 8; 19 and Exs. A-C attached thereto; 27 and Ex. A attached thereto; and 25 ¶¶ 30-38 and Ex. A attached thereto). Respondent denies this finding but provides no evidence in support thereof.

Respondent did not write or put into place any procedures governing his own review of the detailed trading information that he received, and of the trading and market making activities of the Florida Branch, to ensure that the Florida Branch was complying with Kettler & Co.'s markup policy and the federal securities laws. (Div. Exs. 9; 25, ¶ 45; Tr. p. 117). Respondent denies this finding but provides no evidence in support thereof.

During the period July 19 through July 29, 1988, Respondent never made any attempt to limit Forman's activities in connection with the secondary market trading in Windy City securities. Specifically, Respondent took no action designed to: (1) slow down or limit the price increases in Windy City common stock; (2) determine the markups in Windy City

common stock; (3) limit markups on Windy City common stock; or (4) supervise Forman's market making activities or the selling activities in the Florida Branch in any way. (Tr. p. 155). Respondent denies this finding but provides no evidence in support thereof.

During the period July 19 through July 29, 1988, Respondent never discussed with Forman: (1) the volume of activity in Windy City securities; (2) the bid and ask prices of Windy City securities; (3) the increase in price in Windy City common stock; (4) the fact that Kettler & Co. charged increasingly higher prices for Windy City common stock while Kettler & Co. continued to purchase the stock for $.10 per share; or (5) Kettler & Co.'s markups for Windy City common stock. (Tr. pp. 152-154). Respondent denies this finding but provides no evidence in support thereof.

CONCLUSIONS OF LAW

Respondent argues that his rights were violated by the holding of an ex parte hearing. There was no ex parte hearing held in this case. The parties were advised that the hearing would commence February 21, 1995 and it did commence at that time. Respondent failed to appear, but his attorney appeared and conducted a defense for part of the hearing and than exited himself without explanation and/or the agreement of this Office or his adversary.11/

11/ As indicated, the Respondent did not appear at the hearing. His counsel did appear and represented his client. However, no oral or written proofs were offered or received into evidence from Respondent during the course of the hearing. A recess was called at 1:05 p.m. on February 21, 1992. It was agreed by counsel that the trial would resume at 1:30 p.m. At the conclusion of this recess, Respondent's counsel requested a further recess to argue a motion for a temporary restraining order before the Federal District Court.

(continued...)

Respondent argues that the SEC lacks jurisdiction inasmuch as Kettler & Company unconditionally withdrew its license as a broker dealer prior to the start of these proceedings. The Commission has by order dated March 13, 1995 already rejected that argument, indicating that the instant proceeding is against Paul C. Kettler, individually for his failure to supervise under 15 (b) (6) of the Exchange Act. The order states in part: "we may sanction a person associated with a broker dealer at the time of his alleged misconduct if such person has committed or omitted any act or omission enumerated in subparagraph ... E ... [of paragraph (4) (of subsection 15(b)]". Section 15(b)(4)(E) of the Exchange Act relates to a failure to supervise.

Respondent argues that his supervision of Forman was reasonable. The evidence, as discussed below, is overwhelming that Respondent was fully knowledgeable as to the magnitude of illegal price manipulation that was perpetrated in his Florida office. His arguments to the contrary are not factually part of the record of this case. Respondent's reliance on SEC v. Geon Industries, Inc., 531 F.2d 39 (2d Cir. 1976) is inappropriate inasmuch as the Geon court was dealing with a supervision issue absent "red flags".

From approximately July 19, 1988 through July 29, 1988, Forman willfully violated Section 17(a) of the Securities Act of 1933 (Securities Act), Section 10(b) of the Exchange

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11/(...continued)
Respondent's motion was granted, and it was ordered that the hearing was to commence again at 2:15 p.m. At 2:15 p.m., Respondent's counsel failed to appear, and at 2:32 P.M. a note was received from Respondent's counsel to the effect he would not be returning to the courtroom. No further explanation was provided. (Tr. pp. 97-102) The Division thereupon put in the record the rest of its proof. By letter dated April 4, 1995, Respondent's counsel, for the first time to this Office, addressed the matter of his unexplained failure to return mid-hearing. He states, "I was directly instructed by my client not to further attend the hearing".

Act and Rule 10b-5 thereunder, and willfully aided and abetted Kettler & Co.'s violations of Section 15(c) of the Exchange Act and Rule 15c1-2 thereunder in that he caused Kettler & Co. to make false and misleading statements to purchasers of Windy City common stock, caused Kettler & Co. to manipulate the price of Windy City common stock and failed to disclose to customers who purchased Windy City common stock that Kettler & Co.:

1. was charging excessive markups;
2. dominated and controlled the market in the stock; and
3. was manipulating the price of the stock.

From approximately July 19, 1988 through July 29, 1988, Respondent failed reasonably to supervise Forman with a view toward preventing his violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, within the meaning of Section 15(b)(4)(E) of the Exchange Act. As part of his failure to reasonably supervise Forman, Respondent failed to institute procedures designed to detect and prevent Forman's violative conduct. Furthermore, Respondent, despite 1) being on notice of prior regulatory concerns regarding possible excessive markups in securities sold by the Florida Branch, and 2) having available to him information from which he could have determined that the Florida Branch was selling Windy City common stock at increasingly higher prices and at markups far in excess of ten percent:12/

1. Made no effort to determine whether Forman was adhering to Kettler & Co.'s markup policy;

12/ As argued by the Division, there is no support for Respondent's argument that the SEC's 10% excess markup standard is inapplicable here.

2. Made no effort to calculate the markups on shares of Windy City common stock that were sold to customers;

3. Made no effort to determine if markups were being disclosed to customers who purchased Windy City common stock;

4. Made no effort to determine why the price of Windy City common stock was rapidly increasing during the first ten days of secondary market trading in July 1988;

5. Made no effort to determine whether the fact that Kettler & Co. dominated and controlled the market in Windy City common stock was causing the price of the stock to be manipulated;13/

6. Made no effort to determine whether the fact that Kettler & Co. dominated and controlled the market in Windy City common stock was being disclosed to customers;

7. Failed to detect and prevent false and misleading statements being made by registered representatives at Kettler & Co. to purchasers of Windy City common stock; and

8. Took no steps to prevent Forman's violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and aiding and abetting violations of Section 15(c) of the Exchange Act and Rule 15c1-2

13/ I agree with the Division that Respondent's argument that Wien's and Greentree's involvement or lack of involvement in the market was not relevant. It is quite apparent from the number of shares controlled by Kettler & Co. and the price manipulations that the competitiveness of the market was subverted.

thereunder.14/

Based on the foregoing, Respondent failed reasonably to supervise Forman with a view toward preventing his violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and his aiding and abetting violations of Section 15(c) of the Exchange Act and Rule 15c1-2 thereunder, within the meaning of Section 15(b)(4)(E) of the Exchange Act.

Having determined that the respondent has been found to have violated the federal securities laws, it becomes necessary to consider what sanctions, if any, would be in the public interest. In assessing a sanction, due regard must be given to the facts and circumstances of each particular case, since sanctions are not intended to punish a respondent but to protect the public interest from future harm. See Berko v. SEC, 316 F.2d 137, 141 (2d Cir. 1963) and Leo Glassman, 46 S.E.C. 209, 211-12 (1975). Sanctions should also serve as a deterrent to others. Richard C. Spangler, Inc., 46 S.E.C. 238, 254 n.67 (1976).

In imposing administrative sanctions, the Commission may take into account such factors as:

> ...the egregiousness of the defendant's actions, the isolated or recurrent nature of the infraction, the degree of scienter involved, the sincerity of the defendant's assurances against future violations, the defendant's recognition of the wrongful nature of his conduct, and the likelihood that his occupation will present opportunities for future violations.

Steadman v. SEC, 603 F.2d 1126, 1140 (5th Cir., 1979), aff'd on other grounds, 450 U.S.

14/ Integral to reasonable supervision "must be adequate follow-up and review when a firms own procedures detect irregularities or unusual trading activity in a branch office . . . ." John H. Gutfreund, Exchange Act Release No. 31554, 52 SEC Docket 4370, 4387 (December 3, 1992).

91 (1981).

Respondent's abdication of supervisory authority for the Florida office, combined with his total disregard of the many "red flags" presented to him regarding the possibility of unlawful trading in Windy City stock, was egregious. Respondent's failure to reasonably supervise Forman allowed Kettler & Co. and Forman to dominate and control the market for Windy City stock, to manipulate the market in Windy City, to charge customers excessive undisclosed markups and to fail to disclose to customers various material facts in connection with their purchases of Windy City securities, notwithstanding many "reg flags". Edwin Kantor, Exchange Act Release No. 32341, 54 SEC Docket 293, 301 (May 20, 1993). Moreover, severe sanctions are warranted based upon Respondent's receipt of records demonstrating the violations. Finally, Respondent has been sanctioned a total of four times by the NASD. One of these sanctions was for failing reasonably to supervise Forman in connection with excessive markups and manipulation. Another sanction was for failing reasonably to supervise a registered representative. This demonstrates that the failure to supervise in connection with the Windy City IPO was not an isolated incident, but was part of a larger, more severe problem. Respondent's arguments are insubstantial that: (1) his lapses from supervision were short in duration; (2) he received little or no financial gain; (3) public interests were never harmed; and (4) that the facts of this case have never been adjudicated before.

Accordingly, the Division requests and I consider it reasonable that the Respondent receive a particularly strong sanction in the form of a permanent bar from association with a broker-dealer in both a supervisory and a proprietary capacity, and a bar from all association

with a broker-dealer, with the right to reapply, in a nonsupervisory or a nonproprietary capacity, after five years. Such sanctions are consistent with at least two recent cases.

One such case is Albert Vincent O'Neal, Exchange Act Release No. 34116, 56 SEC Docket 2447 (May 26, 1994). In that case, the Commission found that the branch manager, O'Neal, had failed reasonably to supervise a registered representative subject to his supervision. The registered representative had violated the antifraud provisions of the federal securities laws by engaging in various fraudulent sales practices. The Commission noted that O'Neal had: (1) been warned in advance that the registered representative was engaging in possible sales practice violations; (2) been receiving numerous reports that would have alerted him to these fraudulent sales practices; and (3) had failed to conduct any inquiries after receiving these reports. The Commission then stated as follows:

> Under Section 15(b)(4)(E), the test is whether O'Neal's supervision was reasonably designed to prevent the violations at issue, not . . . whether, if all the many other supervisory functions he performed were taken into account, his overall supervisory performance somehow earned him a hypothetical passing grade.

O'Neal, 56 SEC Docket at 2456. The Commission concluded that the O'Neal's supervision was grossly deficient, and barred him from the securities industry, with a right to reapply in a non-proprietary, non-supervisory capacity after one year. O'Neal, 56 SEC Docket at 2457.

The present case is very similar to the O'Neal case. Respondent was warned in advance of the Windy City IPO that Forman might be selling securities at excessive markups. Once the secondary market trading in Windy City began, Respondent was receiving numerous reports on a daily basis that should have alerted him to the violative conduct occurring in the Florida Branch. Finally, Respondent, despite receiving these reports, made

no inquiries concerning the rapid increase in the price of Windy City common stock. In addition, in O'Neal, there were no facts in the record indicating that O'Neal had a prior history of regulatory sanctions. In the present case, Respondent has been sanctioned on four previous occasions. Thus, a more severe sanction than that imposed in the O'Neal matter is warranted.

In John J. Cox, Exchange Act Release No. 33577, 55 SEC Docket 3219 (February 3, 1994), Cox, a principal of a broker-dealer who was also the vice president in charge of compliance, consented to finding that he knew or should have known that the broker-dealer, through its president and its head trader, were engaging in violations of Section 10(b) of the Exchange Act and Rule 10b-6 thereunder.15/ Specifically, the Commission found that the broker-dealer, in selling shares of stock to the public, had failed to disclose to customers, among other things, that: (1) the broker-dealer had exclusive access to 100 percent of the stock at prearranged prices; (2) the broker-dealer dominated and controlled the market in the stock; and (3) the prices charged for the stock had little or no relationship to independent market forces of supply and demand. Cox, 55 SEC Docket at 3223. The Commission then found that Cox failed to conduct any compliance review, which would have alerted him to the fraudulent activity. Consequently, the Commission found that Cox had failed reasonably to supervise the head trader and imposed a sanction of a permanent bar from the securities industry. Cox, 55 SEC Docket at 3224. Respondent argues, without supporting authority,

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15/ Cox consented to the entry of an Order Making Findings and Imposing Sanctions without admitting or denying the findings therein, pursuant to an Offer of Settlement which the Commission accepted. Such an Order is not binding as precedent, but is instructive on the issue of appropriate sanctions in the public interest.

that Cox and O'Neal are dissimilar because the involved violations of long duration.

Similar to the findings in Cox, Respondent in the present case failed to conduct any review which would have alerted him to the manipulation of Windy City common stock in the secondary market, as well as the excessive markups charged to customers. As in O'Neal, there was no allegation or finding in Cox concerning prior disciplinary history, whereas the Respondent has a disciplinary history which includes past findings of failures to supervise. Such a finding in the instant case thus warrants a more severe sanction.

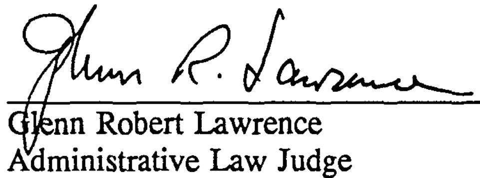
Based on the foregoing, I find that the Respondent, Paul C. Kettler, be sanctioned in the form of permanent bar from association with a broker-dealer in both a supervisory and a proprietary capacity, and a bar from all association with a broker-dealer, with the right to reapply, in a nonsupervisory or a nonproprietary capacity, after five years.

ORDER

IT IS ORDERED that Paul C. Kettler, pursuant to Section 19(h) of the Exchange Act, be remedially sanctioned in the form of a permanent bar from association with a broker-dealer in both a supervisory and a proprietary capacity, and a bar from all association with a broker-dealer, with the right to reapply, in a nonsupervisory or a nonproprietary capacity, after five years. This sanction is imposed as necessary or appropriate in the public interest, for the protection of investors.

Pursuant to Rule 17(f) of the Rules of Practice, this initial decision shall become the final decision of the Commission as to each party who has not, within fifteen days after

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



Glenn Robert Lawrence
Administrative Law Judge

Washington, D.C.
June 27, 1995