

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of :
RALPH M. NORDSTROM :
(M.L. FALLICK & CO., INC.) :

INITIAL DECISION

Washington, D.C.
February 21, 1975

Max O. Regensteiner
Administrative Law Judge

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APPEARANCES: Delano S. Findlay, of the Commission's Salt
Lake City Branch Office, for the Division of
Enforcement.

Ralph M. Nordstrom, pro se.

BEFORE: Max O. Regensteiner, Administrative Law Judge

In these public proceedings instituted by the Commission pursuant to Sections 15(b) and 15A of the Securities Exchange Act of 1934, the issues for consideration in this initial decision are whether Ralph M. Nordstrom engaged in misconduct as alleged by the Division of Enforcement, and, if so, what if any remedial action is appropriate in the public interest.^{1/}

The Division alleges that in 1973, when Nordstrom was vice-president of Western Funding, Inc. ("registrant"), a registered broker-dealer in Minneapolis, Minnesota, he participated in certain transactions involving the improper use of a customer's account and securities. By such conduct, it is alleged, he willfully aided and abetted violations of antifraud, recordkeeping and securities-possession provisions of, and rules under, the Exchange Act. The Division further alleges that Nordstrom failed reasonably to supervise with a view to preventing such violations.

At the hearings, Nordstrom appeared pro se. He cross-examined some of the Division's witnesses, but chose to offer no evidence in his own behalf. After the Division filed proposed findings and conclusions and a supporting brief, Nordstrom responded with a short letter stating his contentions. The Division in turn filed a reply brief.

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

^{1/} The order instituting the proceedings named several other respondents, including M.L. Fallick & Co., Inc. and Western Funding, Inc., both registered broker-dealers, and Wilfred H. Williams. As to all respondents other than Nordstrom the proceedings have been disposed of pursuant to settlement offers submitted by them. While the findings in this initial decision refer to the above-named former respondents, those findings are made for the purpose of determining the issues with respect to Nordstrom and are not binding on those former respondents.

The Respondent

Nordstrom first entered the securities business in 1967. After working for several other firms as a trader, he joined registrant in that capacity in the fall of 1972. Shortly thereafter, and well before the events which led to the charges against him, he became vice-president and a director of registrant. At or about the end of 1973, he left registrant's employ.

The Alleged Misconduct

The misconduct with which Nordstrom is charged relates to a series of transactions set in motion in June 1973 by Wilfred H. Williams, a friend of Nordstrom's and a trader employed in the Minneapolis office of M.L. Fallick & Co., Inc. ("Fallick").^{2/} Fallick was either out of compliance with the Commission's net capital rule (17 CFR 240.15c3-1) or on the verge of noncompliance. In order to improve the firm's net capital position, Williams purported to sell 2,000 shares of Northern Instruments, Inc. ("Instruments") stock from Fallick's trading account to the account of a purported customer named O'Day for a total price in excess of \$25,000. Williams had created the O'Day account for this purpose. And the transaction was what is known as a "park", a device designed to circumvent the requirement of the net capital rule that a deduction of 30 percent from the market value of securities in a broker-dealer's inventory be taken in computing its net capital position.

^{2/} Fallick's principal place of business was Salt Lake City, Utah.

Thereafter Williams took further steps for the apparent purpose of obfuscating the true nature of the transaction. These involved the use of an account maintained with registrant by one Richard Schillinger. On or about June 12, 1973, Schillinger, then a Fallick customer, had transferred some of his securities out of his account with Fallick and to registrant, at the suggestion of a vice-president of Fallick.^{3/} His Fallick account remained open, however.

On or about June 21, 1973, Williams exchanged the Instruments stock in the O'Day account for 4,000 shares of Empire Associates, Inc. ("Empire") stock owned by a company named Seagull, Inc. The Instruments stock was substituted for the Empire stock as collateral for a bank loan to Seagull. Shortly before that exchange, on June 19, Williams told Nordstrom to purchase the 4,000 shares of Empire stock and to place them in the Schillinger account at registrant. The transaction, which was effected at \$6.25 per share, had not been authorized by Schillinger. Williams' uncontradicted testimony is that Nordstrom did not ask him whether he had Schillinger's permission, that he did not tell Nordstrom he had such permission, and that he told Nordstrom he would "guarantee the loss if any." According to Williams, the transaction was a further "park." He further testified that he "parked" the stock in the Schillinger account because he did not think registrant had "the money to park it any more than we did," i.e., had adequate capital to carry the stock in its trading account.

^{3/} While separate accounts in the names of Schillinger and his wife were maintained both at Fallick and registrant, the record shows that all were in fact Mr. Schillinger's accounts. The Schillinger accounts at each firm are accordingly referred to herein in the singular.

On July 1, 1973, Williams terminated his association with Fallick. The following day, Nordstrom sold the Empire stock back to Fallick, purportedly as a "sell out" because Schillinger had not made payment. The market price had declined and the sale was effected at \$5.75 a share, resulting in a \$2,000 loss in the Schillinger account. Registrant paid this amount to Fallick, which in turn reimbursed registrant with a check for \$2,813.50, comprising the \$2,000 plus commissions on both purchase and sale. Thus, despite Williams' departure from Fallick, his guarantee was honored, and registrant and Nordstrom received commissions on the transactions.

One other pertinent transaction remains to be described. On June 21, 1973, Williams caused 3,000 shares of Electric Reel Corporation of America, Inc. stock to be delivered out of the Schillinger account with registrant to Fallick, which in turn caused them to be delivered to the bank as additional substitute collateral for the Seagull loan. Schillinger had not authorized this transaction, either. As of the time of the hearing, the securities had not been restored to him.

Based on the transactions and circumstances recited above and on evidence, discussed below, pertaining to Nordstrom's supervisory responsibilities with registrant, the Division proposes that I find, as alleged, that Nordstrom willfully aided and abetted violations of

1. the recordkeeping provisions of Section 17(a) of the Exchange Act and Rules 17a-3 and 17a-4 thereunder^{4/}, in that registrant's records pertaining to the Empire transactions were falsified to give the appearance

^{4/} 17 CFR 240.17a-3 and 4.

that those were customer transactions when, as Nordstrom knew, they were in fact principal transactions between him and Williams;

2. the antifraud provisions of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder,^{5/} by his unauthorized use of the Schillinger account and conversion or misappropriation of the Electric Reel securities; and

3. Section 15(c)(3) of the Exchange Act and Rule 15c3-3 thereunder,^{6/} by failing to maintain and failing to cause registrant to maintain physical possession or control of fully-paid securities (the Electric Reel stock) carried for Schillinger's account.

In addition, as noted, the Division claims that Nordstrom failed to exercise reasonable supervision with a view to preventing the above violations.

Nordstrom, for his part, asserts that the Schillinger account at registrant was "set up" by Williams; that Williams had often had accounts with him in other persons' names; that, when Williams told him to buy the Empire stock for Schillinger's account, it was "a normal transaction between the two of us and there was no indication that it was anything but that"; that the only benefit he derived from the transaction was the commissions he received; and that he had no knowledge of Fallick's intentions or problems. Nordstrom further asserts that his primary function with registrant was that of trader and that it was Philip Anderson, registrant's president, who supervised the daily recordkeeping, while he (Nordstrom) maintained or prepared the firm's financial records, such as the general

^{5/} 17 CFR 240.10b-5.

^{6/} 17 CFR 240.15c3-3.

journal and the monthly balance sheet and profit and loss statement.

The Empire Transactions

The record leaves no doubt as to the true nature of the Empire transactions, or that the manner in which they were reflected in registrant's records was false. ^{7/} The question before me, however, is whether Nordstrom was or should have been aware of those matters. In my judgment, the evidence compels the conclusion that Nordstrom knew these were not legitimate customer transactions. ^{8/} It is true that the fact that Schillinger had transferred securities from Fallick to registrant only a few days before the Empire transactions could have lent a touch of plausibility to the placing of a buy order by Williams with registrant on Schillinger's behalf. And Williams did testify that on other occasions, prior to Nordstrom's association with registrant, he had opened customer accounts with the firm with which Nordstrom was associated and directed Nordstrom to effect transactions in those accounts. But the record does not indicate whether those were actual customer transactions or other instances of "parking," a practice in which Williams had admittedly engaged a "good number" of times. In any event, the original Empire transaction was on its face not a "normal" one. Any thought Nordstrom

^{7/} Certain of those records were introduced as exhibits, including memoranda of brokerage orders, copies of confirmations and Schillinger's account statement which must have reflected his ledger account. Other records which registrant was required to maintain under Rule 17a-3 and which were also allegedly inaccurate were not so introduced, but the only reasonable inference that can be drawn is that the Empire transactions were also reflected in those records as customer transactions.

^{8/} Williams did testify that Nordstrom had told him shortly prior to the hearing that he had not known the purchase of the Empire stock was a "park". Another witness, who as a Commission compliance examiner had investigated the matters discussed herein, testified that Nordstrom made a statement to the same effect to him. In view of the compelling circumstantial evidence to the contrary, I do not credit those denials.

may have had that the transaction was a customer transaction must have been dispelled when Williams told him he would guarantee any loss on the transaction. ^{9/} As Williams testified, any trader would be likely to recognize a transaction of this nature as a "park."

If any further evidence be needed that Nordstrom recognized the transaction for what it was, it is found in the manner in which it was handled by registrant. Schillinger did not receive copies of the confirmations that were prepared and was not otherwise advised of either the purchase or sale of the Empire stock. No demand was made on him for payment before the stock was sold out. And Fallick's payment of the \$2,813 to registrant was credited to Schillinger's account, as though it had come from him. The record shows, in this connection, that, contrary to Nordstrom's contention, he had supervisory responsibility for registrant's recordkeeping.

As a participant in the Empire transactions, Nordstrom was responsible for the inaccuracies in registrant's records relating to those transactions. I find, therefore, that he willfully aided and abetted violations of Section 17(a) of the Exchange Act and Rule 17a-3 thereunder. ^{10/}

^{9/} When asked whether it was normal for traders to guarantee a loss on "another customer's" brokerage transactions, Williams replied "No, but this was a park." (Tr. 90)

^{10/} However, the allegation that he willfully aided and abetted violations of Rule 17a-4 is dismissed. That rule requires the preservation for specified periods of records required to be prepared. The Division introduced no evidence that records were not preserved. Its apparent theory that the maintenance of inaccurate records results in violations of both Rules 17a-3 and 4 is inconsistent with the position taken by the Commission concerning the relationship of the two rules. See L.C. Fisher Company, Inc., Securities Exchange Act Release No. 10259 (June 29, 1973), 2 SEC Docket 81, 82.

I further find that Nordstrom, by his use of the Schillinger account in the Empire transactions, willfully aided and abetted violations of the antifraud provisions of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. The use of a customer's account without authorization is wholly at odds with a broker-dealer's obligation to deal fairly with his customers. Although, as apparently was the case here, the customer may not suffer actual damage from the unauthorized use of his account, such misuse creates a potential for embroiling him in problems not of his making. Here, for example, Schillinger was subjected to the risk of being asked to pay for stock which he had not ordered or for the apparent \$2,000 net loss resulting from the Empire transactions. And, assuming the requirements of Regulation T of the Board of Governors of the Federal Reserve System^{11/} were observed by registrant, the sell-out of the Empire stock without prior payment^{12/} subjected the account to certain restrictions.

Insofar as the allegation of supervisory failure pertains to the Empire transactions, there is no warrant for an adverse finding in light of the Commission's determination in a recent case^{13/} that where

^{11/} 12 CFR 220.

^{12/} In such a situation, 12 CFR 220.4(c)(8) in substance prohibits further purchases for a period of 90 days from the purchase in question unless there are sufficient funds already in the account.

^{13/} Charles E. Marland & Co., Inc., Securities Exchange Act Release No. 11065 (October 21, 1974), 5 SEC Docket 313, 315.

findings of substantive violations are made against an individual who is an active participant in the misconduct involved, "it is unnecessary to find him responsible for a failure of supervision with respect to the same misconduct."

Electric Reel Stock

The facts pertaining to the delivery of the Electric Reel stock out of the Schillinger account are to some extent shrouded in mystery. As noted, Williams caused the stock to be delivered out, but his testimony does not indicate with whom he dealt at registrant, if anyone. An undated document found in registrant's possession purports to be a request by Schillinger and his wife to deliver the stock to Fallick. And stock receipt forms included in registrant's records show that the securities were delivered to a Fallick employee. The Schillingers testified that ~~the~~ purported signatures on the delivery request were forged. The uncontradicted testimony of Anderson shows that Nordstrom had the responsibility for supervising and did supervise the cashier,^{14/} whose duties included the receipt and delivery of securities. Anderson himself was not aware of the delivery until after these proceedings were instituted.

The Division, while asking me to find that Nordstrom willfully aided and abetted violations of Rules 10b-5 and 15c3-3 in connection with this transaction, concedes that the evidence that he personally authorized

^{14/} Nordstrom and the cashier had both worked for another firm previously and she had been hired by registrant on Nordstrom's recommendation.

or knew of it is inconclusive. Indeed, the record does not provide a basis for such a finding. But the Division's further argument that Nordstrom failed reasonably to supervise registrant's back office with a view to preventing a misappropriation of Schillinger's securities is in my opinion supported by the record. Assuming that Nordstrom was not aware or apprised of the delivery when it occurred, he would have become aware of it upon a proper review of the Schillinger account. Such discovery would have led a reasonable supervisor to pursue the matter further, since the delivery out of the account of securities which had only been delivered into the account a few days earlier and which had not been sold was on its face questionable. A simple inquiry addressed to Schillinger would have disclosed that he had not authorized the transaction. Prompt action could then have been taken to make Schillinger whole.^{15/}

Public Interest

The misconduct which I have found Nordstrom engaged in was of a serious nature. His unauthorized use of a customer's account in order to accommodate a friend and the consequent falsification of registrant's records reflect a failure to appreciate the responsibilities of a person engaged in the securities business toward his customers and an indifference to important regulatory requirements. Moreover, Nordstrom must have been aware that by his participation in a "parking" transaction he was contributing to an attempted deception of the regulatory authorities and the

^{15/} Cf. Cortlandt Investing Corporation, 42 S.E.C. 709, 715 (1965).

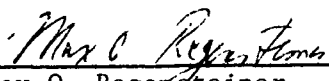
subjection of Fallick's customers to financial risk.

It is my conclusion, under all the circumstances, that it is in the public interest to bar Nordstrom from association with a broker-dealer, with the proviso that after nine months he may apply for permission to become so associated in a nonsupervisory position. ^{16/}

Accordingly, IT IS ORDERED that Ralph M. Nordstrom is hereby barred from association with a broker or dealer, provided that after nine months he may apply to the Commission for permission to become so associated in a nonsupervisory position, upon an adequate showing that he will be properly supervised.

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

Pursuant to that rule, this initial decision shall become the final decision of the Commission as to each party who has not filed a petition for review pursuant to Rule 17(b) within fifteen days after service of the initial decision upon him, 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.



Max O. Regensteiner
Administrative Law Judge

Washington, D.C.
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^{16/} All proposed findings and conclusions submitted by the parties have been considered, as have their contentions. To the extent such proposals and contentions are consistent with this initial decision they are accepted.