

**UNITED STATES OF AMERICA**  
**Before the**  
**SECURITIES AND EXCHANGE COMMISSION**

**INVESTMENT ADVISERS ACT OF 1940**  
**Release No. 2936 / October 16, 2009**

**ADMINISTRATIVE PROCEEDING**  
**File No. 3-13653**

**In the Matter of**

**TOBIAS BROS. INC.**

**Respondent.**

**ORDER INSTITUTING ADMINISTRATIVE  
AND CEASE-AND-DESIST PROCEEDINGS,  
PURSUANT TO SECTIONS 203(e) AND  
203(k) OF THE INVESTMENT ADVISERS  
ACT OF 1940, MAKING FINDINGS, AND  
IMPOSING REMEDIAL SANCTIONS AND A  
CEASE-AND-DESIST ORDER**

**I.**

The Securities and Exchange Commission (“Commission”) deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 (“Advisers Act”) against Tobias Bros. Inc. (“Tobias Bros.” or “Respondent”).

**II.**

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the “Offer”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over it and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Sections 203(e) and 203(k) of the Investment Advisers Act of 1940, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order (“Order”), as set forth below.

### III.

On the basis of this Order and Respondent's Offer, the Commission finds<sup>1</sup> that

#### Summary

These proceedings concern unauthorized trading by Ethan Kass ("Kass") who caused and concealed at least \$8.4 million in losses to investors in five investment advisory accounts managed by Tobias Bros. ("Circle T"). Between February and May 2005 while employed by Tobias Bros. as an order processing clerk, Kass executed and concealed at least 24 unauthorized trades resulting in multi-million dollar trading losses to Circle T investors. In July 2005, Seth Tobias, the principal and the sole owner of Tobias Bros., fully reimbursed all injured investors for these losses.

Despite Kass's attempts to conceal his unauthorized conduct, Tobias Bros. and Seth Tobias failed to perform their supervisory functions and missed a number of red flags that should have alerted them to Kass's unauthorized trading. For example, each day Tobias Bros. generated internal risk reports which were provided to Tobias Bros. supervisors. This report listed Circle T's securities holdings and profit and loss as of the prior trading day, including, on certain dates, Kass's unauthorized trades. However, Tobias Bros. supervisors, including Seth Tobias, at times, failed to even review these reports and therefore missed an opportunity to detect Kass's unauthorized trading and protect Circle T from the resulting losses. Tobias Bros. supervisors also missed other opportunities to detect Kass's unauthorized trading. They routinely failed to review reports that captured Kass's deletions and re-entries of his unauthorized trades from Tobias Bros.'s portfolio management system. Moreover, Tobias Bros. failed to monitor Kass's activities at the firm in accordance with the procedures set forth in its own compliance manuals.

#### Respondent

1. **Tobias Bros. Inc.**, is a Delaware corporation established in December 1995. It is an investment adviser registered with the Commission since 2004 and reportedly has approximately \$68 million under management currently. It also was a broker-dealer registered with the Commission from 1998 until February 2, 2008. Tobias Bros.'s main office is located in New York, New York, and during the relevant period, it had branch offices in Pennsylvania and Florida. Seth Tobias owned Tobias Bros. until his death in September 2007.

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<sup>1</sup> The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

### **Other Relevant Persons**

2. **Kass**, age 28, resides in New York, New York. Kass began working as an intern at Tobias Bros. in 2002. He was promoted to an order processing clerk in 2004. Kass does not hold any securities licenses. Tobias Bros. terminated Kass's employment in June 2005.

3. **Seth Tobias**, resided in New York, New York until his death on September 4, 2007. Seth Tobias held Series 7, 24, and 63 licenses, and was the sole owner and principal of Tobias Bros. and other related entities since 1996. He was not an investment adviser registered with the Commission, but acted as the investment adviser to the five unregistered investment funds that suffered the losses from Kass's unauthorized trading.

### **Background**

4. Between February and May 2005 (the "Relevant Period"), Kass executed at least 24 unauthorized trades that caused the Circle T funds to incur approximately \$8,474,325 in losses. Kass concealed his unauthorized trades in at least two ways. First, Kass did not enter these trades in Circle T's handwritten trade blotter. Second, Kass disguised his trading activity by manipulating the related trade data that he did enter into Tobias Bros.'s internal portfolio management system. Neither Kass nor Tobias Bros. profited from Kass's unauthorized trading. In July 2005, Seth Tobias fully reimbursed these investors out of his own pocket for these losses.

### **Failure Reasonably to Supervise Kass**

5. As a supervisor at Tobias Bros., Seth Tobias oversaw regulatory compliance and daily operations at the firm. He was directly responsible for supervising Kass with regard to the processing of trades on behalf of Circle T. Yet, Seth Tobias and Tobias Bros. ignored its own compliance procedures, missed numerous red flags and otherwise unreasonably failed to detect Kass's unauthorized trading and concealment scheme. For example, Tobias Bros. failed to review numerous trade reconciliation reports created independently by its prime broker, as well as internal Tobias Bros. reports, which often included evidence of Kass's unauthorized trades.

6. During the Relevant Period, Tobias Bros. identified both Seth and Samuel Tobias, Seth's brother and another portfolio manager, as "supervisors" and designated Samuel Tobias as the supervisor of, among other things, "error reports...trade confirmations...and trade reporting, generally." Similarly, in connection with the investment advisory business, Tobias Bros. identified Seth and Samuel Tobias as "managers" who were "responsible for supervising the activities of all associated persons," and stated that "[g]enerally, Sam[uel] Tobias will be responsible for correcting trading errors..." In practice however, Samuel Tobias's supervisory responsibilities were limited to those accounts that he managed - not the Circle T funds, which were the responsibility of Seth Tobias.

7. Tobias Bros. maintained a proprietary internal portfolio management system to track its trades and transmit those trades to its prime broker. This portfolio system captured, among other things, real time position information, purchases and sales, and profits and losses

(“P&L”). Once the clerk entered the trade into the portfolio system, the trade is instantaneously viewable on the portfolio manager’s computer screen, and reflected in the portfolio system’s P&L.

8. At the end of each trading day, Kass used this portfolio system to transmit Circle T’s daily trading data to its prime broker. The prime broker also received trade confirmations from other brokers reflecting trades executed by Tobias Bros., and confirmed those trades with the executing broker. The prime broker provided by fax a “trade break report” to Tobias Bros. at the start of each trading day. This report reflected any discrepancies noted by the prime broker based on its comparison between trades reported by Circle T and trades reported by executing brokers purportedly done on behalf of Circle T.

9. Tobias Bros.’s procedures required certain designated personnel to review the trade break and similar reports and reconcile any discrepancy with the prime broker. Trades that could not be reconciled would continue to appear on the trade break report until the prime broker and Tobias Bros. reached a resolution. The prime broker also made available online a report which showed each trade reported and executed on behalf of Circle T.

10. In February 2005, upon the retirement of the operations manager for Tobias Bros., Seth Tobias gave Kass additional assignments to review trade discrepancies as reported by the prime broker and to resolve those discrepancies directly with the prime broker, functions previously performed by the retired operations manager. Kass’s dual functions relating to order entry and order reconciliation allowed him to make unauthorized trades and to conceal those trades from inattentive supervisors, a significant internal control flaw that he routinely exploited to the detriment of the Circle T funds.

11. As part of his fraudulent scheme, Kass entered his unauthorized trades into the portfolio system for transmission to Tobias Bros.’s prime broker after the market closed and subsequently deleted the trades from the system before trading commenced the next day. Portfolio managers, who relied on the information to manage Circle T’s P&L during the trading day, would therefore be ignorant of any trade discrepancies, unless they scrutinized and compared the prime broker’s trade records against those generated by the portfolio system – both of which Tobias Bros. assigned Kass to reconcile.

12. In addition, the portfolio system created a report called the “deletion report” that listed all changes made to any trading information, including additions to, or deletions from, existing positions. The deletion reports show Kass’s additions and subsequent deletions of his unauthorized trades. Tobias Bros. supervisors could have identified instances of Kass’s unauthorized trading had they reviewed the deletion reports. However, certain Tobias Bros. supervisors claimed that they were unaware that the deletion report even existed until after Kass’s unauthorized trades had come to light.

13. Tobias Bros. and Seth Tobias also failed to properly review daily reports generated internally by Tobias Bros. to manage risk and P&L exposure in the Circle T and other managed accounts. Tobias Bros. prepared these reports daily, based on information maintained by the prime broker, and emailed them at the start of each trading day to Seth Tobias and other Tobias Bros.

portfolio managers. These daily risk reports provided the portfolio managers with various statistics, including P&L information, securities holdings, and year-to-date valuation, among other trade-related information. In a section entitled “Portfolio Statistics,” the daily risk reports clearly showed instances of Kass’s unauthorized trades because the report reflected the trading that Kass reported to the prime broker, but which Kass later deleted from certain of Tobias Bros.’s internal books and records. Seth Tobias admitted that he did not review the daily reports at all on certain days, although he received them. He confirmed that had he reviewed the reports he would have noticed the “red flag” caused by Kass’s unauthorized trading, especially if that trading significantly increased Circle T’s holdings of certain securities.

14. As a result of the conduct described above, Tobias Bros. failed reasonably to supervise Kass, within the meaning of Section 203(e)(6) of the Advisers Act, with a view to detecting and preventing Kass’s violations of Section 10(b) of the Securities Exchange Act of 1934, and Rule 10b-5 thereunder, and aiding and abetting violations of Sections 206(2) and 204 of the Advisers Act, and Rule 204-2 thereunder.

### **Failure to Maintain Books & Records**

15. Section 204 of the Advisers Act and Rule 204-2 thereunder require an investment adviser to make and keep true, accurate and current certain books and records relating to its investment advisory business. During the Relevant Period, Tobias Bros. failed to maintain accurate books and records.

16. Tobias Bros.’s books and records were inaccurate as to its investment advisory business due to Kass’s unauthorized trading. Tobias Bros.’s books and records, including trade blotters and portfolio management system, did not accurately reflect Kass’s unauthorized trades and subsequent deletions.

17. In addition, Tobias Bros. failed to preserve instant messages which contained Kass’s unauthorized trades as it was required to do by the Advisers Act and its own compliance procedures. Tobias Bros.’s investment adviser procedures at the relevant time stated that: “[a]ll electronic communications are viewed as written communications, and the SEC has publicly indicated its expectation that investment advisers retain all electronic communications for the required retention periods. If a method of communication, such as e-mail or instant messaging, lacks a retention method, then it must be prohibited from use by the Firm.”

18. Despite these prohibitions, in early June 2005 Tobias Bros. discovered that Kass used instant messages to place unauthorized trades with a broker-dealer on behalf of Circle T. Tobias Bros. failed to archive such communications and none of Kass’s supervisors ever monitored his use of instant messages to route the orders, even though Seth Tobias admitted that he knew certain Tobias Bros. personnel used instant messages for business purposes.

19. As a result, Tobias Bros. willfully violated Section 204 of the Advisers Act and Rules 204-2(a)(3) and 204-2(a)(7) thereunder.

### **Tobias Bros.'s Remedial Efforts**

20. In determining to accept the Offer, the Commission considered remedial acts promptly undertaken by Respondent and cooperation afforded the Commission staff.

#### **IV.**

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in Respondent Tobias Bros.'s Offer.

Accordingly, pursuant to Sections 203(e) and 203(k) of the Advisers Act, it is hereby ORDERED that:

- A. Respondent Tobias Bros. is censured.
- B. Respondent Tobias Bros. cease and desist from committing or causing any violations and any future violations of Section 204 of the Advisers Act and Rules 204-2(a)(3) and 204-2(a)(7) promulgated thereunder.

By the Commission.

Elizabeth M. Murphy  
Secretary