ADMINISTRATIVE PROCEEDING
FILE NO. 3-4647

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of

FIRST CALIFORNIA CO., et al.

INITIAL DECISION

Washington, D.C.
May 20, 1976

Jerome K. Soffer
Administrative Law Judge

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APPEARANCES: Michael H. McConihe and Burton W. Wiand, of the Washington, D.C. Regional Office of the Commission, for the Division of Enforcement.

Albert W. Thomson, of Linde, Thomson, Van Dyke, Fairchild & Langworthy, for M. J. Coen.

BEFORE: Jerome K. Soffer, Administrative Law Judge

This public proceeding was instituted by the Commission's order issued April 8, 1975, as thereafter amended, pursuant to sections 15(b) and 15(A) of the Securities Exchange Act of 1934 (Exchange Act), naming as respondents: First California Company (FCC), M. J. Coen (Coen), and Harold F. Smither (Smither).

The Order for Public Proceeding (Order) alleges the following with respect to the respondents:

A. That during the period from on or about January, 1971 to on or about September, 1971, FCC and Coen willfully violated Sections 5(a) and 5(c) of the Securities Act of 1933 (Securities Act) in the offer and sale of common stock of Westgate-California Corporation (Westgate).

B. That during the period from on or about January, 1971 to July, 1973, FCC and Coen willfully violated and willfully aided and abetted violations of Sections 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, in connection with the offer, purchase, and sale of Westgate common stock and of the subordinated capital notes of United States National Bank of San Diego (USNB).

C. That Coen willfully aided and abetted violations by Westgate of Section 13(a) of the Exchange Act and Rule 13a-1 thereunder, in the filing of false reports by Westgate of Form 10-K for the years 1969 through 1973.

D. That during the period from June 1969 until November 1973, Smither willfully violated and aided and abetted violations of Section 17(a) of the Securities Act involving embezzlement, fraudulent conversion, and misappropriation of funds and securities, and that Smither was convicted of a felony violation upon a plea of guilty in the United States District Court for the District of Oregon on March 15, 1975, involving the described conduct.

E. That during the period from June, 1969 until November, 1973, FCC and Coen failed reasonably to supervise Smither with a view to preventing his commission of the described violations.

F. That on August 28, 1973, Coen consented to the entry of an order in the United States District Court for the Southern District of California, permanently enjoining him from violations of the securities laws in connection with the offer, purchase, and sale of securities of Westgate, USNB, or any other security.

The Order directed that a public hearing be held before an Administrative Law Judge to determine the truth of the allegations set forth and what, if any, remedial action is appropriate in the public interest and for the protection of investors.

On August 5, 1975, the Commission issued an order against Smither, based upon his default in answering the Order, barring him

from associating with any broker or dealer (SEA Rel. No. 11570). On October 3, 1975, the Commission issued an order, based upon the consent of FCC neither admitting or denying the allegations, finding that FCC had willfully violated the securities laws, as alleged, and revoking its registration as a broker-dealer (SEA Rel. No. 11707).

A public hearing was held with respect to the sole remaining respondent, Coen, before the undersigned Administrative Law Judge on September 17, 18, and 19, 1975 in San Francisco, California, and on October 15, 16, and 17, 1975 in San Diego, California. Thereafter, proposed findings and fact, conclusions of law, and supporting briefs were filed by counsel for the Division of Enforcement and for respondent Coen, including a reply brief filed by the Division. The findings and conclusions herein are based upon a preponderance of the evidence as determined from the record and upon observation of the demeanor of the witnesses.

Respondent Coen, a resident of Kansas City, Mo., has been involved in stock brokerage and corporate financing for more than thirty years. His securities activities include the ownership and operation of Midland Securities, Inc. (Midland), a broker-dealer with principal offices in Kansas City until early 1971, when it merged in and became a branch of FCC, a company in which he had become controlling stockholder and Chief Executive Officer. Coen also was a director of Westgate from 1963 to 1968, and has been a general partner in an

investment company known as First Greystone Associates (Greystone). He is presently the sole stockholder of a corporation which figures in these proceedings, British Columbia Investment Company (BCIC). Other companies in which he had or has an interest and which are involved in the transactions hereinafter described include Golconda Corporation (Golconda), Elsinor Royalty Company (Elsinor), Kernville Brokerage Company (Kernville), Missouri Western Realty Company (Missouri Western), and Dormik Development Company (Dormik), in all of which he at one time or another was officer, director, and/or stockholder.

Prior to the revocation of its registration, FCC was a registered broker-dealer for many years with its principal office in San Francisco, California. At one time it had as many as 400 employees who were stockholders of the organization and maintained about 40 offices in a number of Western States. It was a member of the Pacific Coast Stock Exchange.

Smither had been employed by FCC from 1962 until August 31, 1973. Between March and August, 1973, he was the chief operating officer at the San Francisco headquarters. For the years prior thereto, he worked out of the FCC office in Salem, Oregon. He plead guilty to the crime of fraud in the sale of securities involving embezzlement, forgery and misappropriation of funds and securities committed while in the Oregon office of FCC, and was sentenced on March 15, 1975 to serve a term of 6 months imprisonment and 5 years probation thereafter (U.S.A. v. Smither,

USDC, Ore., Cs. No. 74-9).

The one individual who is central to all of the events, activities and transactions which underly the Division's basic case herein is Mr. C. Arnholt Smith. Smith is a San Diego banker who was the founder, chairman and controlling stockholder of USNB as well as of Westgate until 1973. Other individuals involved in the transactions, as pertinent hereto, include Phillip Toft and Edward P. Schroeder, Jr., associates of Smith, and Flora Jackman and Ronald Sutter, trusted employees. Corporations controlled by Smith and his associates and involved in the relevant transactions include U.S. Holding Co. and Sovereign States Capital Corporation (SSC). There are also numerous subsidiary and affiliate corporations of the Smith controlled corporations which enter into these proceedings. Smith, a one-time "San Diego Man of the Year", enjoyed a prestigious position in that community. Coen had been associated with him in various business ventures for more than 20 years.

Westgate was incorporated in Nevada in 1960 and maintained its principal offices in San Diego. It is a conglomerate that has operated in the past through numerous subsidiaries involved in such businesses as seafood processing, real estate, fresh produce, public surface and air transportation, insurance, and hotel operations. It is currently undergoing reorganization under Chapter XI of the Bankruptcy Act. Its Class A Common Stock is registered with the Commission pursuant to Section 12(g) of the Exchange Act and is publicly held.

BCIC, also with offices in San Diego, is a holding company operating through numerous subsidiaries. Its operations, between 1969 and 1973, were managed by Smith and his associates Toft, Schroeder and Jackman. At the present time, stock ownership is in the name of Coen but is held by a trustee and is subject to the jurisdiction of the United States District Court in San Diego.

USNB is a national bank with its principal office in San Diego. Smith was the beneficial owner of more than 30 per cent of its capital stock, and, until 1973, he controlled its operations. At that time, the bank was declared insolvent and placed in receivership under the jurisdiction of the Federal Deposit Insurance Corporation. By May, 1973, its deposits had exceeded one billion dollars, it had sixty-three branches in Southern California, and was the ninth largest bank in California and eighty-seventh in size in the nation.

The Scheme to Inflate Earnings - The "Monster Project"

Basic to the charges in the order for proceedings herein is the allegation that a scheme was entered into intended to arbitrarily inflate the earnings of Westgate and USNB by causing these entities to engage in sham transactions with the assistance of nominee parties among whom Coen was included. That such a scheme existed is found in the testimony of Schroeder, who was group controller and responsible for the accounting functions of a number of Smith-controlled and Smith-affiliated companies including U.S. Holding Company, SSC, Westgate, and

numerous of their subsidiaries.[1] The scheme, which had its beginnings in 1962, was entered into by Smith, Toft, Westgate's Executive Vice-President, and Sutter, Westgate's Vice-President and controller. The plan involved the purchase and sale of assets between Westgate and apparently independent, but actually controlled corporate entities, at inflated values, with the payments for purchase price and debt service accomplished by advances of funds from USNB. It was determined to be necessary to conceal from Westgate auditors the fact that the transactions were between related parties. This concealment was accomplished by use of third party nominees acting as stockholders, officers, and directors of the various shell subsidiaries and affiliates in order to give the appearance of bona fide arms-length negotiations and dealing.

This scheme embraced the so-called "Monster Project" involving the transfer of ownership of the various USNB bank branch real properties out of the numerous subsidiary corporations by which they were owned into Westgate by December 31, 1970. These transfers were accomplished by a series of bookkeeping transactions whereby the properties were first transferred to BCIC and thence to Westgate. However, when the auditors for Westgate challenged the appraisal values assigned to

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1/ For example, SSC had some twenty to thirty affiliates and U.S. Holding Company some four to ten subsidiaries whose primary business was the ownership of real estate that was occupied as bank branches of USNB. The designated principals of these companies included Smith and various of his close relatives, such as daughter-in-law, a former wife, and an older brother.

the properties and questioned whether they involved related parties, Westgate rescinded the sale and transferred the properties back to BCIC sometime in March of 1971. USNB loaned the money to BCIC needed to repay Westgate.

All of the paper work involved in these transactions was handled by Schroeder active under the direction of Smith and Toft. However, in order to give the appearance of arms-length negotiations the nominal ownership of BCIC was caused to be placed in John Roth and Warren Metcalf, officials of a St. Joseph, Mo. bank, who had no other function with BCIC but to lend their names and to sign documents without question, in return for a small sum of money. Their involvement, which began in 1969, was indirectly procured by Coen.[2/] They paid $450,000 for the BCIC stock, wholly financed by USNB, which they held until September of 1971 when this note was taken over by the Coen-controlled company, Dormik, who sent Roth some $12,000 as his profit in the transaction. At no time did they have any knowledge of BCIC's operations, including the period when the bank properties were transferred back and forth, or that Dormik was buying them out 2 years later. From time to time, they were sent papers and documents from the Smith employees in San Diego for signing which they did without knowing what they meant. These documents embraced confirmations to auditors of Westgate concerning various transactions to the effect that they were executed on an

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2/ They were introduced to the deal by a Coen business associate, Edwin B. Wright, who learned of it from Coen. At one point, Roth expressed the opinion that during the time he was nominal owner of BCIC, Coen seemed to know more about its business affairs than he, Roth. Both men were long time friends and associates.

arms-length basis.[3/]

The acquisition of control of BCIC by Coen through Dormik was financed entirely by USNB. Operations continued to be managed by Schroeder and the Smith group in San Diego with very little involvement by Coen. Nevertheless, in February of 1972, Coen caused to be certified to the auditors of Westgate that a total of eight transactions between BCIC and Westgate, relating to real estate and over 125,000 shares of USNB stock, occurring between March 31, 1971 and June 30, 1971, were arms-length transactions. These were the same transactions previously certified by Hunter.

3/ Roth and Metcalf were not the only straw men Coen introduced to the Smith-dominated scheme. There was Charles H. Hunter, a Kansas City real estate broker, who, under the promise that he would handle the brokerage in the sale of the USNB branch properties, willingly allowed himself to become an officer and director of some twenty BCIC subsidiaries, as well as of the Coen-owned Kernville Brokerage Co., M. V. Independence, Inc., and Coronado Fisheries, Inc. He signed numerous documents, such as vessel purchase agreements, mortgages, evidences of debt, etc., usually sent to him from Coen's office, in complete ignorance of what he was signing. Under the direction of Sutter, Hunter also signed confirmations attesting to arms-length transactions for Westgate's auditors in August 1971 as the vice-president of BCIC, although he had no information prior thereto that he was elected to this office. He remained as a straw man until September 11, 1972.

Another "front" man Coen introduced to the Smith-dominated transactions is John Bertoglio, a Kansas City real estate developer. He became involved in some multi-million dollar Westgate real estate transactions wholly financed by USNB. The property eventually wound up in the hands of a Hunter-owned corporation, Pepperland, also with total financing by USNB. It is interesting to note that Bertoglio, for one, refused to comply with requests for confirmations to Westgate's auditors that these were arms-length transactions.

Despite the fact that each of these transactions were paper transactions handled entirely by Schroeder and by the Smith organization in San Diego, and financed in full by USNB, Coen (like Hunter before him) in actual ignorance of these deals, undertook to confirm that there was no financing of any of the transactions, that the sales prices were determined as a result of arms-length negotiations, and that BCIC was completely independent of Smith, Westgate, U.S. Holding Company, or USNB. As reported in the Form 10-K filed by Westgate for 1971, the effect of the transactions confirmed by BCIC was to increase the assets and earnings reported by Westgate, before taxes, by $289,223.

Another aspect of the "Monster Project" embraced transfers of ownership of eleven tuna fishing vessels and two merchant ships, the majority interest of which were owned by two Westgate subsidiaries, Coronado Fisheries, Inc. and M. V. Independence, Inc. In 1969, Elsinor Royalty Company was organized by Smith and his associates, naming Coen as the incorporator, for the purpose of acquiring remaining minority interests, one of whom was Smith's daughter, and thence to be transferred to Westgate. Funds were advanced by USNB to Elsinor, the intermediary utilized. Because auditors of Westgate questioned the value of the assets involved, the transaction with Elsinor was rescinded, and on June 1, 1971, Elsinor purchased Westgate's interest in Coronado and M. V. Independence for some $6,300,000 using monies advanced by

by USNB through two BCIC subsidiaries. Until this point, although Coen was named the incorporator, the stock was actually held by SSC, another Smith controlled corporation. On September 1, 1971, the stock was formally transferred from SSC to the Coen-owned Midwestern Realty Company, with monies borrowed from BCIC to pay SSC. Although all of these transactions were handled by Schroeder and the Smith employees in San Diego, Coen, nevertheless confirmed, in February, 1972, to Westgate auditors that the purchases of the stock of Coronado and M. V. Independence took place as a result of arms-length negotiations, that Elsinor was independent of the control of Smith or his affiliates, and that there was no financing involved in the transaction. The effect of these transactions, as reported on Westgate's Form 10-K for 1971, was to increase its assets and earnings by $78,000.[4/]

Kernville was organized by Smith and his associates, naming Coen as one of its incorporators, whose stock was, like the Elsinor shares, formally transferred to Coen's Midwestern Realty in September 1971, with money borrowed from USNB. During 1970, Kernville

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4/ Coen's testimony with respect to his involvement with Elsinor varied at different states of the proceedings. At one time, he stated that Elsinor was formed for him in 1969 and he was then the owner thereof. He later changed his testimony to the effect that he was merely an incorporator, without his knowledge, and it was not until September 1, 1971, that he acquired actual ownership from SSC. Nevertheless, he undertook as early as December, 1970 to confirm to auditors of Westgate that his Midwestern Realty Company was the owner of the Elsinor stock.

purchased some 2,100 acres of cattle ranchland from Westgate for $3,210,000, all but $10,000 of which was paid through borrowings from SSC and USNB. Despite the fact that this transaction was handled entirely by Schroeder and other Smith associates, without any knowledge or participation by Coen, he nevertheless, on May 19, 1971, confirmed to the auditors of Westgate that Midwestern was the actual owner of Kernville, that neither Smith, his affiliates, Westgate, nor any of its subsidiaries directly or indirectly entered into the transaction, or had any interest therein. The effect of this transaction was to increase Westgate's earnings, as reported on its 1970 Form 10-K, by $2,079,000.

Dormik, a shell corporation owned by Coen, had been used from time to time as a conduit of funds from USNB in order to pay Westgate or SSC for purchase of other corporations, such as Kernville, Westwood Realty, Elsinor and BCIC. One such transaction, involving a loan of some $620,000 occurred on September 1, 1971.

On December 31, 1969, Dormik purchased 1,040 acres of California land from Westgate for $1,560,000 which was totally financed by USNB. The bank was also the source of funds to service the debt and to pay the property taxes first advanced by SSC. In response to the Westgate's auditors request on January 30, 1970, a Coen employee, acting pursuant to his guidance and instructions, confirmed the sale but withheld the fact that the financing was done through USNB. Subsequently, on March 27, 1970, Coen personally confirmed to Westgate's auditors

that no affiliate of Westgate had any direct or indirect interest in the said transaction, thereby withholding from them the fact that the financing was done by USNB and SSC, both commonly controlled along with Westgate by Smith. According to Westgate's 1969 Form 10-K, this transaction increased its sales and earnings by $1,039,000.

Further instances of false confirmations follow. On December 31, 1969, Continental Western Corporation, a company owned in principal part by Greystone, purchased from Westgate the control stock of an airline operator known as Aero Commuter, and borrowed $2,750,000 from USNB and/or Valley National Bank of Phoenix, Arizona to do so. Negotiations for the loan were handled by Coen through Smith or Toft. Nevertheless, on March 24, 1970, Coen confirmed to the auditors of Westgate that no director, officer or affiliate of Westgate had any direct or indirect interest in this transaction, thereby concealing from them the fact that USNB had advanced funds to Continental Western, with which to purchase Aero Commuter from Westgate. According to the Westgate's records, it purchased Aero Commuter for $275,000 just ten months prior to its sale for ten times as much to Continental Western. Moreover, Aero Commuter was operating at substantial losses. The effect of the transaction was to increase Westgate's 1969 sales and earnings, as reported in its Form 10-K by $653,000. In addition, Westgate was relieved of owning a losing asset.

On April 1, 1971, Westgate sold to BCIC a 50% interest in the Maria Hill Joint Venture, in which it owned half and the remainder was owned by Smith's former wife. The purchase price of $500,000 was financed completely by USNB. In February of 1972, by which time Coen had become the nominal owner of BCIC, he caused his employees to confirm to the auditors of Westgate that there were no notes or any financing, particularly by USNB, Smith, or affiliates, in connection with the transaction. As reported in the 1971 Form 10-K by Westgate, this transaction had the effect of increasing its earnings by $162,300.

On December 29, 1971, a subsidiary corporation of BCIC known as Arriendos De Ponce, Inc. purchased from a subsidiary of Westgate its interest in certain construction contracts for two tuna boats being built in Puerto Rico for the sum of $2,446,958. The monies were borrowed entirely from SSC. On February 23, 1972, Coen caused to be confirmed to the auditors of Westgate that the purchase price was determined at arms length, that BCIC was independent of Westgate, USNB, or Smith, and that there was no financing in connection with the sale.

Additional transactions of the type described above include the following: On March 31, 1971, Missouri Western, which otherwise had no assets and the stock of which was owned by Coen, acquired from Westgate some 63,000 shares of USNB stock, using money advanced by SSC. Between March 31, 1971 and June 1, 1971, BCIC purchased a number of securities from Westgate representing shares of such Westgate subsidiaries as

Southern Counties Realty, Cuyamaca Land Company, Bonsall Highlands Estates, Keystone Brokerage, Socal Properties, Santa Maria Ranches, Westgate-California Development, Inc., and 125,047 shares of USNB stock. The selling price varied from a low of $57,000 for the Cuyamaca Land Company stock to more than $3,600,000 for the USNB stock (of which more than $2,114,000 represented an assumed note). All of these purchases were done with money advanced by USNB or SSC. Nevertheless, shortly after February 9, 1972, Coen caused his employees to confirm to the auditors of Westgate the very same confirmations made with respect to all the other properties and assets described above: that there was no financing for the transactions, that they were negotiated at arms length, that they were ~~indifferent~~ independent of Smith, etc.

The Forms 10-K filed with the Commission by Westgate, pursuant to Section 13(a) of the Exchange Act for each of the years 1969 through 1972 show that the various transactions described above were handled as cash sales of assets. In other words, they were shown as a sale of a particular property and the receipt of the cash paid therefor. These financial reports do not show that the sources of the funds used by the purchasers was a bank commonly-owned with Westgate or that the transactions were with or through Smith-dominated shell corporations. Thus, it does not appear therein that the dealings were among related parties and entities.

The 1970 10-K report contains an advisory by the firm of certified public accountants preparing the financial data that the reported

information is in material respects based upon the accuracy of representations, advice, or other confirmation made by or on behalf of interested persons. Reference is made in several explantory notes contained in the report to transactions between Westgate and Coen-owned corporations, particularly to the sale of 2,140 acres of land to Kernville, and described as (Note 4), "a newly created corporation controlled by Mr. M.J. Coen". Note M of the report also relates that over the years there were a number of profitable transactions between Westgate and Coen controlled companies, including the sale of Aero Commuter to Continental Western in 1969.

In similar vein, the 10-K report for 1971 contains the same advisory as to reliance upon confirmations by the auditors, and refers to a number of transactions with Coen in that year as having been negotiated at arms length. The report refers specifically to the acquisition of the fishing vessels by Elsinor and of USNB stock by Missouri Western, as well as the various transactions with BCIC, herein before related. Note O of this report contains this statement: "In the opinion of management, Mr. Coen is independent of Westgate and the transactions were at fair values determined by arms-length negotiations."5/

During the early investigatory phase of these proceedings, Coen purported to testify with respect to all of the transactions as if he had personal knowledge of them. However, at the hearing herein,

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5/ As a shareholder in Westgate, Coen received copies of its financial statements for the years 1969 through 1972 including the notes referred to above.

he conceded that in replying to all of the confirmations to the auditors of Westgate whether involving Kernville, BCIC, Elsinor, Missouri Western, Dormik, etc., he consulted with Schroeder, Smith or Toft as to how to answer them. He claims that he relied upon the word of these gentlemen, having known and trusted them for many years. Concededly, he had no basic information of his own as to the financing, details of the negotiations, etc.[6/] Coen further concedes that "in hindsight" confirmation statements to the effect that Smith, Westgate, or their affiliates were not involved in the various transactions were wrong.

Coen insists that his willingness to lend himself to the practices described was based upon an understanding with Smith that the bank properties were being assembled into one entity in order to form a "real estate investment trust", and the tuna vessels into another entity to become the basis of a tax-shelter type of offering, both to be administered in some way by Coen. In fact, by September of 1971, the ownership of the bank properties was entirely in BCIC. Coen claims that for the next four months he made some attempts to organize an REIT by, for example, negotiating with Smith to increase the rentals paid by the USNB

6/ In fact, Schroeder was under strict orders from Smith to tell Coen (or anyone else) very little or nothing about the transactions in which they were being used.

branches.7/ In February 1972, Coen underwent heart surgery and upon his release from the hospital, an investigation into these affairs had already been begun by the Commission. He thereupon told Schroeder and Smith to sell out all of his interests. Schroeder did, in transactions the details of which Coen has no recollection, then dispose of all of the properties held by BCIC and Elsinor to various individuals, including many business associates of Coen. However, Coen continues to own the stock of BCIC.

The Acquisition of First California Company

As stated, FCC was an employee-owned registered broker-dealer with numerous offices in western United States. Its affairs were run by various employee committees, including a Management Committee. By early 1970, FCC found it desperately necessary to find new capital in order to meet the net capital requirements and the almost daily demands of the Pacific Coast Exchange. A principle subordinated debt holder, with an investment of about $1,000,000, would only advance

7/ At no time did Coen seek information concerning the individual subsidiary companies and the bank buildings which they owned, their value, or the mortgages thereon, nor did he examine the books and records of any of these companies in order to determine their financial condition. Although at one time Elsinor owned all of the vessels in the tuna fleet, by the time that Coen completed his purchase of Elsinor in 1971, five of the vessels had already been transferred out by Schroeder to various other corporations. In the latter part of March 1972, Schroeder conveyed out the remaining six vessels of the fleet to other corporations without the knowledge of Coen. It is clear, therefore, that if there were going to be an REIT or a tax exempt tuna fleet, Coen was not going to control it or even have much to say in the matter.

additional capital on terms deemed unsatisfactory to the employee Management Committee. With the approval of Smith, USNB made a loan of $600,000 on February 3, 1970 to FCC. The capital deficiencies continued and Smith again came to the rescue with a further agreement whereby Westgate advanced $600,000 to replace the USNB note, and an additional $1,000,000 of capital in return for which it or its nominee would be able to purchase 51% of the stock of FCC. About a month after this advance, Smith regretfully advised that Westgate would have to withdraw from the transaction because banking regulations prohibited an affiliate of a national bank from owning a brokerage firm. He asked that the FCC management find replacement capital.

Sometime in September of 1970, Smith made Coen aware of the opportunity to buy out Westgate's interest in FCC, promised that USNB would advance him the capital required to make the purchase, and then made FCC aware of Coen's interest. The FCC management, unable to obtain other capital, agreed to the substitution of Coen for Westgate. Coen, who previously had operated a single broker-dealer firm in Kansas City, now had become, through the intercession and financing of his long-time associate, Smith, the majority owner and president of a large, widely operating broker-dealer. Midland, after a few months merged into and became the Kansas City Branch of FCC. Coen spent most of his time at the Kansas City office and continued the same type of committee management and general operation that had

existed prior to his taking over, including the services of a compliance officer, Mr. Arthur Lewis. Coen advised the management that he expected strict compliance with the rules and regulations of the various regulatory agencies.

From time to time, it became necessary that FCC obtain additional capital and over the next three-year period some $3,925,000 was infused through Coen, as subordinated or equity capital. Of this amount, $2,650,000 was borrowed from USNB by Coen-controlled corporations. There was an additional $1,375,000 contributed by relatives of Smith, or friends and associates of Coen whose loans and guarantees were arranged for by Smith.8/

On October 5, 1973, FCC sold its retail operations to Roberts, Scott and Company, a registered broker-dealer and New York Stock Exchange member, who took over the accounts of those customers wishing to be so transferred. The remaining accounts of FCC were eventually paid all credit balances and received all securities.

The Sale of Westgate Stock

Shortly after Coen took over FCC, he arranged a meeting in San Diego between officials of Westgate, on the one hand, and, on the other, the supervisory sales personnel of FCC in order to familiarize employees with Westgate's activities, real estate holdings, and other of its properties. At one of these meetings officials of USNB addressed

8/ One of these individuals, a Mr. Korholz, loaned FCC $450,000, and when FCC could not make good on its note, Coen purchased the note from him.

the sales personnel.

Coen was a general partner in Greystone, an investment company which had included among its holdings approximately 260,000 shares of Golconda Corporation. Since the shares were not marketable ("control" stock), and since Greystone was in great need of cash, Coen offered the stock to Smith in an "investment letter". Smith, in turn, offered to exchange an equivalent amount of allegedly marketable Westgate stock then held by BCIC,[9] and Coen agreed. The BCIC holdings embraced 273,750 shares of the Class A Common Stock of Westgate which represented about 17% of the total of such class in circulation. Coen was evidently concerned about the marketability of the Westgate stock since he personally asked both Smith and Toft "many, many times, if the stock they were talking about was free and tradeable" and they assured him it was.[10] Still wanting further assurance, Coen insisted upon a letter to the same effect. (At that time, BCIC was nominally owned by John Roth but Coen did not think it necessary to inquire of him about the tradeability of the stock, since Roth was in no position to know.)

On December 8, 1970 a letter was written addressed to Midland signed by Flora Jackman as Vice-President of "British Columbia Investors Limited" (there is no such company by that name) and containing a blanket but unsupported confirmation that the involved shares of Westgate

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9/ Actually, the shares were held by an SSC subsidiary, but they were transferred to BCIC as a step to effect the exchange transaction. SSC is a Smith-controlled corporation whose stock was held by his daughter-in-law.

10/ Transcript, page 539

did not constitute "control" stock and was "free" stock. The exchange took place, and after Greystone acquired the 273,000 Westgate shares from BCIC, it first sold, at Coen's direction, 131,000 to Midland (Coen's brokerage company just prior to its merger into FCC) as a principal, which then sold them to FCC, also as a principal. The time elapsing between the transfer from Greystone to Midland to First California could have been as short as one day or as much as a week. Coen personally advised and encouraged the sales personnel of FCC to promote the sale of the Westgate stock, and shortly thereafter some 131,000 shares were sold by FCC to the investing public.

Still concerned as to the tradeability of the Westgate stock, Coen then obtained the opinion of his counsel, Albert Thomson, Esq. who, in a letter dated January 12, 1971, makes the general unsupported conclusion concerning "41,884" shares of the Westgate stock as follows: "Based upon the letter of British Columbia Investors Limited of December 8, 1970, it is our opinion that the Westgate stock may be freely sold by you without registration." Mr. Thomson was not requested to, nor did he, make any independent investigation as to the marketability of the shares.[11/] Moreover, the reduced number of shares for which he was certifying would indicate that, during the intervening period between December 8, 1970 and January 12, 1971, sales were made of the rest of the shares obtained from BCIC. All but approximately 43,000 shares

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11/ Interestingly, Coen did not consult the compliance officer of FCC, who gave the opinion at the hearing that an offer to sell a block of stock in excess of 10% of the outstanding shares of that class would constitute an underwriting required to be registered.

were disposed of by Greystone in similar fashion through FCC. The stock was sold to the public at about $7.00 per share. It presently has little, if any, value.

The Sale of USNB Subordinated Capital Notes

From time to time, FCC had sold the stock of USNB to its customers. Coen had suggested to the sales personnel and management of FCC that they recommend such securities as a good investment for appropriate retail customers. FCC maintained a file on the bank which included among other things its financial reports.

At a March 1973 meeting in San Diego, Smith, in response to a remark by Coen or one of his employees that they would be interested in merchandising bank securities, advised that he knew of some USNB 8-year, 7 1/2 per cent interest, subordinated notes that were available for sale at the Valley National Bank, in Phoenix, Arizona. Coen had become aware earlier, in the latter part of November or in December 1972, that USNB had issued some $6 to $10 million worth of similar capital notes, which were offered by Smith to FCC and others as an underwriting, but in which it did not participate. He later learned from Smith, sometime in January or February of 1973, that those notes had been disposed of privately to unnamed people or institutions, and that he, Smith, had "taken some down himself". During the March 1973 conversation in San Diego, Smith did indicate that the notes available at the Valley National Bank were part of the placement done in the

Fall of 1972. He did not state to whom these notes belonged. Coen claims not to have asked but to have assumed they belonged either to the Valley National Bank or to its customers. He further asserts that he did not associate the notes to be sold with those taken down by Smith only several months previously.

When FCC and its officials decided to undertake the sale of the USNB notes, Smith advised them to bill for earned commissions to Valley National Bank, attention of Dean Smith, care of C. Arnholt Smith at the USNB in San Diego. Coen claims that there was nothing unusual about these instructions and saw no reason to inquire as to why notes which were being ostensibly sold by a Phoenix bank on behalf of its customers had to be billed in this way.12/

Thereafter, in April of 1973, FCC obtained from Valley National Bank and then disposed to its customers some $2 million worth of the USNB subordinated notes. This was shortly followed by the sale of another $2 million worth of them. Then, the Commission instituted civil injunction proceedings against certain parties including FCC and Coen. In connection therewith, FCC signed a consent degree in which it agreed among other things, to disclose the true owner of securities of USNB or Westgate that it may sell.

12/ In the opinion of Mr. Edmund W. Carlson, FCC's financial vice-president, it was rather unusual to seek payment of commissions from one other than the actual seller of such securities. However, he raised no question since his instructions to get the commissions from Smith in San Diego came from Coen, his superior.

Then, Coen asked and Smith advised that there were additional USNB notes from the same source. Coen and FCC then arranged for a fifth million dollars worth of notes to be sold. At this point, Smith revealed that he was, in fact, the owner of the USNB notes, which Coen claims is the first knowledge that he had of this fact. After FCC sold $212,000 worth of the last batch of notes, he was informed by a representative of this Commission that a Cease and Desist Order had been entered into involving Smith and the U.S. Comptroller of the Currency which was not being disclosed to purchasers.[13/] This was

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13/ The Cease and Desist Order was entered into, on consent, on May 24, 1973, which directed, among other things, that Smith resign as a director of USNB, that the Bank would make no further loans to Westgate or its subsidiaries, and that Smith would not sell any shares of stock of the Bank owned by him. This order was not made public. Thereafter, as a result of the filing of an injunction proceeding by this Commission against Smith, Westgate and others, the Acting Comptroller of the Currency issued a press release on May 31, 1973, as follows:

> "The Board of Directors of U.S. National Bank, San Diego, and Mr. C. A. Smith have consented to the issuance of a cease and desist order by the Office of the Comptroller of the Currency under which the bank is taking the steps necessary to achieve the orderly collection of the loans presently held by the bank which represent a concentration of credits to Westgate California Corporation, and other related companies and to limit any further loans to these entities. Pursuant to the order, Mr. Smith has agreed to indemnify the bank against losses in connection with such loans. To date, the bank has experienced no losses in connection with such loans.
>
> These arrangements were made by the Acting Comptroller in cooperation with the Securities and Exchange Commission."

In view of the contents of the notice of charges which resulted in the consent order, and of the terms of the order itself, this release by the Comptroller was innocuous in the extreme.

Coen's first knowledge of that order. Thereupon, FCC ceased any further sales and sent a purported rescission letter dated June 29, 1973 to the purchasers of the last batch (but not to previous buyers) which advised that Smith was the owner of the notes and that USNB and the U.S. Comptroller of Currency had entered into "an agreement".[14/] This notice was accompanied by a glowing letter from the then President of USNB portraying a very favorable future for the bank. The FCC letter then suggested to those customers not satisfied with their investment to contact the Vice-President of FCC.[15/] It is not known how many of the purchasers acted with respect to this letter. The USNB notes are presently worthless.

The Final Transactions

Following the close of FCC operations and the transfer of accounts to Roberts, Scott, and Company on October 5, 1973, FCC was engaged primarily in winding down its affairs and settling claims and accounts. Claimants for its remaining capital included certain individuals who had filed suits against it, subordinated lenders, and the shareholders-employees of the company. Coen caused FCC to engage in one further transaction: the purchase in a private placement from Sunmaster Manufacturing Company of 300,000 of its shares of stock at

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14/ The words "cease and desist order" were not mentioned.

15/ The so-called "rescission" letter contained no offer or invitation to rescind.

a price of $.50 or $.60 per share. At that time Coen was Chairman of the Board of Sunmaster and his wife was a stockholder. The shares were not tradeable, and price did not reflect the book value of the stock. This transaction enabled Sunmaster to obtain needed working capital. It is contended that subsequently, FCC sold from 120,000 to 130,000 of its Sunmaster shares, although the circumstances of that transaction are not stated.

Smith has been showing a continuing interest in purchasing the shares of BCIC now held by Coen. As stated, Coen is the beneficial owner of the stock which is being held in trust by Mr. Raymond F. Bjorkquist and subject to the jurisdiction of the U.S. District Court in San Diego. Coen was in active negotiation with Smith for the sale of these shares only several weeks prior to the San Diego hearing in this proceeding, as a result of which his attorney sent a detailed letter to Smith's attorney outlining specific terms and conditions for such a sale. Smith offered to relinquish multi-million dollar claims against Coen in return for the stock.[16/]

16/ Coen, in his testimony on October 16, 1975, withheld telling of the existence of these active negotiations and, in fact, testified that he had no intention at that point of doing so. After learning that "Judge Nielsen" (Hon. Leland C. Nielsen, U. S. District Judge) would have no objection to the filing of a request for permission to sell the stock, Coen testified that he might reconsider selling the stock to Smith although it was not clear in his mind as to whether he still had any intent to sell. He continued to withhold information of the existence of the detailed letter-offer made just a few weeks before. Finally, Coen, in reaction to a story in the local papers, for the first time disclosed on the last day of hearing the existence of his negotiations with Smith and of the letter offer. He thereby hoped to correct any impression in the record that he had not previously discussed such a sale with Smith or any of his representatives.

DISCUSSION AND CONCLUSIONS

The order for proceedings herein charges that the described activities of Coen have involved him in a number of violations of the Securities Laws calling for the imposition of sanctions sufficient to protect the "public interest". Coen concedes that by virtue of the entry of the aforesaid order on August 28, 1973, permanently enjoining him from violations of the Securities Laws, the Commission's jurisdiction to impose sanctions has been established, as indeed it has (Section 15(b)(4)(C) of the Exchange Act). However, he denies having committed any other violation as charged and asks that only the lightest of sanctions be imposed against him.

The Section 5 Violations

Coen has stipulated that, during the period from approximately January to September 1971, he directly and indirectly made use of the means and instruments of transportation and communication in interstate commerce and of the mails to offer to sell, sell, and deliver after sale 230,000 shares of restricted Class A common stock of Westgate California Corporation when no registration statement was in effect as to said securities pursuant to the Securities Act. Unless he can establish that these transactions were exempt from the registration provisions of the Securities Act, he must be held to have violated these provisions.[17/] It is well settled that the burden of proving the

17/ Section 5(a) of the Securities Act provides, in part, that unless a registration statement is in effect as to a security, it is unlawful for any person to sell such security through the means and instrumentalities of interstate commerce. Section 5(c) provides that prior to the filing of a registration statement it would be unlawful to offer to sell such security through the means and instrumentalities of interstate commerce.

availability of an exemption from the registration requirements of the Securities Act rest with the person claiming the exemption (SEC v. Ralston-Purina Co. 346 U.S. 119, 126 (1953); Herbert L. Wittow, 44 S.E.C. 666, 671 (1971)).

Although Coen has not specified the particular statutory exemption relied upon, he does itemize in support of his claim that he did not willfully sell the Westgate securities in violation of the registration laws, the following: that the Westgate stock came from SSC, a corporation owned by Smith's daughter-in-law who was never an officer, director, or controlling shareholder of Westgate (i.e., no common control); that Smith, Toft, and Flora Jackman all advised him that the Westgate stock was free and tradeable; that the certificates for the Westgate shares were in "street names" of all kinds thereby indicating that it was not control stock; and that Greystone still owns 40,000 of the shares. It would be fair to conclude from these allegations that Coen is attempting to rely upon the exemption from registration requirements provided by section 4(1) of the Securities Act to transactions by any person other than an issuer, underwriter, or dealer.

There is no question that the Westgate stock was being acquired from an "issuer" as that term is defined in the Securities Act. The term issuer not only means every person who issues or proposes to issue any security (Section 2(4)), but also "any person directly or indirectly controlling or controlled by the issuer, or any person under direct or

indirect common control with the issuer" (Section 2(11)). It is clear that the person who was in control of Westgate, BCIC, and SSC was Smith, not his daughter-in-law, nor Roth, nor Schroeder, nor Jackman. It is with Smith that Coen arranged for the original transaction by which the Westgate stock was acquired. It is with Smith or one of his cohorts that Coen always did business in regard to Westgate, USNB, BCIC, or SSC. For him to claim that SSC was actually owned by an innocent by-stander, Smith's daughter-in-law, borders on the ridiculous. Smith at all times pertinent hereto totally controlled Westgate, SSC and BCIC along with the individuals who were nominally owners thereof, and Coen knew it.

From the foregoing, it necessarily follows that Coen was acting as an "underwriter" as that term is defined in the Securities Act, meaning "any person who has purchased from an issuer with a view to *** the distribution of any securities ***". Simply stated, an underwriter is one who purchases stock from the issuer with an intent to resell to the public (Quinn and Co. v. SEC, (10th Cir. 1971), 452 F. 2d. 943, 946).

The facts of record establish that Greystone engaged in the transaction for the sole purpose of obtaining needed liquidity to meet its debts and for other purposes. It already owned non-tradeable securities in Golconda. It wanted tradeable and marketable securities to raise money. The purpose of acquiring the Westgate shares was for immediate resale, and the fact that the plan was to pass the stock

first to Midland and then to FCC as principals before selling it to the public does not make any difference. 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 (See Lewisohn Copper Corp., 38 S.E.C. 226, 234 (1959)). Coen, using his previous friendship and business relationship with Smith, together with his position as general partner of Greystone and majority owner and president of Midland and FCC, was the party who engineered the entire distribution to the public from the issuer. This made him an underwriter.

That Coen recognized from the very beginning the situation he was in is apparent from his conduct in connection with the transaction. Firstly, the size of the block of stock involved should have and did put him on inquiry that he was dealing with a control situation involving the issuer of the security. He attempted a sort of investigation but not a meaningful one. He asked Smith, the control person, and his associates "many,many times" for assurance that the Westgate stock was tradeable. Then, still not being sure of himself, he insisted upon a writing to that effect which was given to him on behalf of a non-existent entity by an underling known to be serving as nominal officer or director of the Smith-controlled corporations. All he could hope to get were self-serving statements from the interested parties themselves, none of these efforts complied with the duty owed by a

professional in the securities business dealing closely with the investing public to protect it from illegal offerings.[18/]

Finally, still uncertain of his position and wanting further assurance, Coen obtained from his counsel, after the majority of the stock was dispersed to the public, a meaningless letter merely reiterating and relying upon what Miss Jackman had represented. It shows no background investigation either being requested or having been made.[19/]

From the foregoing, it is concluded that Coen was not interested

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18/ See Stead v. SEC (10th Cir. 1971), 44 F. 2d 713, 716, in which the court pointed out that an inquiry made of the transfer agent by a broker, and the advice received that the stock was "freely tradeable" is not a sufficient inquiry.

19/ Neither Coen nor his counsel made even the most minimal efforts to satisfy themselves that the Westgate stock was exempt from the registration requirements. The duty of a broker-dealer undertaking the distribution of unregistered securities has been spelled out in SEA Release No. 33-4445 (also No. 34-6721), February 2, 1962, and need not be spelled out herein. The following statement therein is significant:

> "There have been a number of cases in which dealers have unsuccessfully sought to justify a claim to exemption under Section 4(1) of the Securities Act simply by securing from the sellers, actual or ostensible, representations that such persons are neither officers, directors, nor large stockholders of the issuer, and submitting such representations to an attorney who then gives an opinion to the effect that assuming the correctness of such representations, exemption under Section 4(1) is available. *** Indeed, if an attorney furnishes an opinion based solely upon hypothetical facts which he has made no effort to verify, and if he knows that his opinion will be relied upon as the basis for a substantial distribution of unregistered securities, a serious question arises as to the propriety of his professional conduct."

in making an investigation as to Smith control, or of the fact that he was participating in the distribution of a security which required registration. Rather does it appear that, in his anxiety to obtain immediate funds needed by Greystone, Coen was merely seeking assurances which could be relied upon should the transaction be challenged later. A finding would be justified that his conduct was "willful" in the classic sense of being done deliberately and intentionally. However, there is no need to so conclude. It is well established that a finding of willfulness under the Securities Act does not require an intent to violate the law; it is sufficient that the person charged with the duty consciously performs the acts constituting the violation. (Billings Associates, Inc. 43 S.E.C. 641, 649 (1967); Hughes v. SEC 174 F. 2d. 969, 977 (C.A.D.C. 1949)). Coen knew what he was doing.

The purpose of the registration requirements of the Securities Act is to protect investors by promoting full disclosure of information thought necessary to informed investment decisions. (SEC v. Ralston-Purina Co., supra, p. 124). Because public policy strongly supports registration, the exemption when relied upon must be strictly construed against those claiming it (Quinn and Co. v. SEC, supra, p. 946). Respondent herein has not sustained such a burden.

Accordingly, it is found that Coen willfully violated the provisions of the Securities Act with respect to the sale of the Westgate stock when no registration statement was in effect as to said securities, as required by the said Act.

Section 13(a) Violations

Coen is charged with aiding and abetting violations by Westgate of Section 13(a) of the Exchange Act[20] and Rule 13a-1 thereunder, in the filing of false reports on Form 10-K for the years 1969 through 1973. The Division contends that the financial reports for 1969 through 1972 were false, by including the "results" (i.e., the profits reported) from numerous "sham" transactions, the details of which have heretofore been described. The aiding and abetting charged to Coen involves the submission by him of the false confirmations to Westgate's auditors endeavoring to verify the details of the transactions, particularly as to whether they involved independent parties and arms-length transactions. No evidence concerning the 1973 report has been presented.

The threshold issue is whether the financial reports filed by Westgate were, in fact, "false" insofar as filing requirements are concerned when they did not disclose that these were transactions among related parties. Coen argues that from Westgate's point of view, the transactions complained of amounted merely to a sale of its assets and the receipt of cash from the purchasers with no further contingencies or strings attached. Under these circumstances, Coen urges that Westgate was perfectly justified in merely reporting the transaction as a cash sale without showing that USNB was the source of the cash. He points to no rule requiring that these transactions be handled differently.

20/ Sec. 13(a), "Every issuer of a security registered pursuant to Section 12 of this title shall file with the Commission in accordance with the rules and regulations as the Commission may prescribe as necessary or appropriate for the proper protection of investors and to insure fair dealing in the security -- ***
(2) such annual reports *** as the Commission may prescribe."

Likewise, the Division refers to no such rule or accounting practice.

Dr. John C. Burton, the Commission's Chief Accountant, testified (Exhibit 2) that there are no Commission or accounting rules of which he is aware dealing specifically with the manner of reporting transactions wherein a company sells an asset for cash and financing is provided to the buyer by an affiliate of that company. He did give his opinion that all transactions should be fairly presented in order to provide information to investors as reflective of the operations of the enterprise and of economic realities. The question of how to deal with non arms-length transactions in financial statements is still a developing area of accounting and capable of varying concepts. The treatment thereof would depend upon a number of factors, and fixed guidelines are not established in all cases.[21/]

From this record, it is concluded that the Westgate auditors were under no lawful obligation to report the transactions other than as they did, even though it would have been more helpful and meaningful if the Smith-related interest and activities had been disclosed. However, as seen, the Forms 10-K for both 1970 and 1971 contain affirmative statements by the auditors that they expressly relied upon the confirmations received from principals (including Coen) concerning the transactions reported, and specifically, that Coen was acting independently

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21/ As a result of an objection made by Division's counsel, Mr. Burton was not permitted to give his opinion as to how many of the transactions in the Westgate California matter should have been reported.

and at arms-length in the transactions with Westgate or its subsidiaries occurring during those years.

There is no question that the described transactions were Smith controlled and directed, using shell corporations and straw men whose purchase money was supplied by Smith controlled USNB. It is undoubted that Coen participated therein when he permitted himself to become such a straw man and by lending his name and reputation to whatever request was made of him by Smith and his crew. In other words, despite the auditors' affirmative statements, these were not arms-length transactions. Hence, the affirmative statements were false. They were asserted in the very financial reports that investors could be expected to rely upon to provide them with the full information necessary to make an informed opinion concerning the securities of Westgate. As such, their content in the reports would tend to defeat the very purpose of which the filing of financial reports was intended. Coen, by filing the false confirmations with the auditors, under the circumstances heretofore described, aided and abetted the submission of this false information for the years 1970 and 1971. Such violations on his part were willful, as willfullness is understood in the securities laws. A man of his business and securities experience had every reason to fully appreciate the purposes for which the confirmations were sought and the effect that the information therein would produce.

Accordingly, it is found that Coen aided and abetted Westgate's violation of Section 13(a) of the Exchange Act in the filing by Westgate

of false and misleading financial data in the Forms 10-K for the years 1970 and 1971. However, the similar charges contained in the order, concerning the years 1969, 1972 and 1973 have not been established.

The Anti-Fraud Charges

The Order for Proceedings charges Coen and FCC with willfully violating and aiding and abetting violations of the anti-fraud provisions of the Federal securities laws with respect to the sale of the Westgate stock and of the USNB subordinated capital notes.

Section 17a of the Securities Act makes it unlawful for any person "in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce, or by the use of the mails, directly or indirectly - "to do any of the following:

"(1) to employ any device, scheme or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances in which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser"

Section 10(b) of the Exchange Act makes it unlawful, in connection with the purchase or sale of any security to use or employ, "any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors."

Rule 10b-5 promulgated thereunder, extends, in effect and with a few language changes, the provisions of 17(a) relating to the sales of securities to both the purchase or sale thereof. The Division contends that Coen violated all three clauses of the anti-fraud provisions cited.

The Division bases its claim that Coen violated the first clause of the anti-fraud provisions - a scheme or artifice to defraud - in the existence since 1962 of the Schroeder-admitted scheme by Smith and Toft to inflate the assets and earnings of Westgate and USNB through a series of transactions financed by USNB funds embracing the use of dummy corporations and straw men. Coen's involvement in the scheme is found not in the inception thereof, but later in his willing and necessary participation therein by lending his name (and suggesting other individuals) to help give the appearance of arms length transactions and by blindly attesting to them by the untrue confirmations sent to the Westgate auditors.[22/]

22/ His protestation that he was not one of the creators of this scheme, or that he was not made aware of it until long after it was started are well-founded. However, his conduct made him a willing participant therein, even though there is an absence of proof of actual knowledge of the scheme itself, since he played an integral role in the fraud charged. Compare Sprayregan v. Livingston Oil Company, 295 F. Supp. 1376, 1378 (D.C., S.D.N.Y., 1968).

The scheme as charged was not entered into and carried out in direct connection with the offer, purchase or sale of the Westgate securities and the USNB notes. It had other motives, probably involving transfer and use of USNB funds to further the interests of Smith and his family members. In order to connect up the scheme to the sale of the securities the Division asserts in its Brief (P. 46) that the results of the scheme were transmitted to the public securities market through Westgate's and USNB's allegedly false financial reports.

In other words, it is not the Smith-Toft scheme that is blamed for the fraud on the public, but rather the reporting of the results thereof in the Forms 10-K filed that is the connection to the purchase or sale of the said securities. It is not even alleged that the filing of false financial statements was part of the scheme as conceived, but that it was only an effect thereof.[23/] Hence, the scheme and the ultimate sale of Westgate or USNB securities has not been linked up.

In any event, this aspect of the situation, insofar as it applies to the sale of the Westgate securities, and the extent to which a violation by Coen of the securities laws was involved therein, has been fully covered in the discussion and findings relating to the Section 13(a) violations hereinabove. It would be repetitious and unnecessary to use the same conclusions as the basis for finding another violation under the first clause of Section 17(a) and Rule 10b-5. The purpose of the act

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23/ In Dienstag v. Bronsen, (C.C.H. ¶92,274, Transfer Binder 1967-69, S.D.N.Y., 1968) relied upon by the Division, the filing of false financial reports was a part of the scheme alleged in the complaint.

to protect the investing public and to secure fair dealing in the securities market apply equally to the reporting requirements as for the anti-fraud requirements.

Finally, any allegation of fraud concerning false or misleading financial reports of USNB, as the basis for charges in connection with the sale of the Bank's notes, has not been sustained. There is no evidence whatsoever as to the contents, true, false or misleading, that may be therein reported. No Section 13(a) charges have been alleged or proved relative to USNB reporting requirements, and no reference made to USNB's reports.

In respect to violations of the second clause of the anti-fraud sections, the elements thereof charged in the order for proceedings were that during the time FCC and Coen sold 230,000 shares of the Westgate Class A stock, they failed to disclose to purchasers the existence of the ongoing scheme and the effect of such scheme upon Westgate's financial reports and, further, that they failed to disclose the true financial condition of Westgate. Coen admits that during the relevant period he failed to make representations concerning the existence of the scheme and that he caused to be disclosed to certain purchasers and potential purchasers the information contained in Westgate's Forms 10-K. He denies, however, that he knew or ever was part of such a scheme. Knowledge of the existence of such a scheme would undoubtedly have influenced a prospective purchaser in making a decision whether to purchase the stock

and, hence, was material. Compare Affiliated Ute Citizens v. U.S., 406 U.S. 128, 153 (1972).

However, it has not been established that Coen, at least by January 12, 1971, the date when it would appear that the stock was sold,[24/] had known of the existence of the scheme. True, he had begun to engage in some of the transactions with Westgate on a few deals in 1969 including the purchase by Dormik of 1,040 acres of land, by Continental Western of Aero Commuter, and by Coen's Sunland Development Co. of some real estate, and one in 1970 when Kernville bought land from Westgate for some $3,200,000. These transactions (except the Aero Commuter sale) were handled exclusively by Schroeder without Coen's knowledge of them.

Coen made no independent inquiry, but, even if he had, it is doubtful that he would have been able to learn of the Smith-Toft scheme either from the principals of from other sources. The San Diego operatives were under strict orders to reveal nothing. Westgate was a large

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24/ The time frame within which Coen sold the Westgate shares was apparently brief. This, despite the allegation in the Order that the period began January, 1971 and ended in July 1973, the allegation in the Division's Brief (P. 48) that the sales were made in 1970, and the stipulation by Coen that sales occurred from on or about January to September 1971. Greystone acquired the 273,750 Westgate shares in early December 1970 in exchange for its illiquid Golconda holdings with the intent of immediate resale in order to raise some urgently needed cash. The stock was an unregistered issue. A number of pass-through transfers from original holder to ultimate seller were made in a short time. By the time Attorney Thomson gave his opinion on January 12, 1971, he was talking about only 42,000 shares which is the amount still remaining in Greystone's hands. Clearly, all or nearly all of the remaining shares were disposed of in the intervening six-week period. (These and the related factors discussed heretofore in connection with the findings of violations of Sections 5(a) and 5(c) might well have formed the basis for an anti-fraud violation. But, they are not so charged.)

and well-known corporate conglomerate whose securities were widely held. Its Form 10-K merely showed the described sales as cash transactions, which, as shown before, did not necessarily violate concepts of proper accounting reporting. At this point, Coen's participation in the scheme would not warrant disbelief on his part as to their accuracy. (The 1970 10-K, which did contain some affirmative false statements concerning arms-length dealings, was not filed until March 31, 1971, after the bulk of the Westgate block of stock was sold.)

Under all of the circumstances, it is concluded that with respect to the sale of the Westgate stock at the time it occurred, Coen neither knew, nor by reasonable inquiry could he have found out about the scheme to inflate the earnings of Westgate, nor has the Division established that the financial reports of Westgate then available to Coen did not show the true financial condition of the Company as it existed at that time. These are the only specifications of anti-fraud violations charged against the Westgate sale. They have not been sustained.

With respect to the sale of the USNB subordinated capital notes, the order charges that between April and July 1973, Smith sold, and Coen participated and assisted in the sale of, $4.2 million of the securities without disclosing: (a) The full circumstances relating to the business practices of USNB, (b) the impact of the fradulent scheme upon the financial condition of USNB, (c) that USNB was carrying millions of dollars

in loans to Coen-held companies, among others, which were of questionable value, (d) that the Comptroller of the Currency had recently issued a Cease and Desist Order with respect to many of the business practices previously engaged in by USNB, (e) that Smith had recently been required to resign as director and officer of USNB, and (f) that C. Arnholt Smith was the seller of the securities.[25/]

By the time Coen was dealing in the USNB capital notes, he and his owned-corporations had been involved in many more USNB financed deals with Westgate and its subsidiaries than when he sold the Westgate stock. True, these were principally done without his knowledge as to the details thereof; but, he was called upon in each case to sign papers in connection therewith, to confirm the falsehoods of arms-length negotiations, of no connection with Smith etc., to Westgate's auditors, and had done other acts relating to these transactions. By this time, also, he had induced others to act in similar straw man capacity for Smith deals. There were articles in the press which were called to his attention, concerning insider transactions by Smith, his bank, and Westgate, in some of which Coen was named. An action had been commenced against him and FCC

25/ In its brief, the Division also tries to tie in the fact that over the years between 1970 and 1972, FCC retailed to its customers several blocks of USNB stock without disclosing the scheme. However, this will be disregarded as not included within the scope of the Order. The brief also charges as a fraudulent omission, the failure of Coen to state in connection with the sale of the notes, that he, FCC, USNB, Smith and Westgate had been named in a suit by the Commission charging fraud in connection with the operations of Westgate and USNB. This also has not been set forth in the Order and will also be disregarded. (Compare International Shareholders Services Corporation, SEA Rel. No. 12389, April 29, 1976, FN 19.)

by the Commission alleging the facts of fraudulent manipulation and dealing, in addition to a civil action which was brought against them concerning the same circumstances. He had, or should have had, enough information to have caused him to make searching investigation as to all of the surrounding circumstances before offering to sell these notes to the public.

Further, Coen either knew, or should have known, or should have made inquiry to learn, that Smith was the seller of the securities. The circumstances surrounding the manner in which FCC was brought into the picture of selling these notes leaves the conclusion either that Coen knew of Smith's ownership but deliberately closed his eyes to this fact in order to help the individual who was directly responsible for his being president and majority stockholder of FCC or, if he did not know, then he did not wish to know. He was aware that Smith, just a few months before, had taken some of the USNB notes for himself. He was told to collect commissions for the sale not from the Valley National Bank, the ostensible seller, but from Smith and USNB. The notes were delivered for sale to FCC, not from the Valley National Bank, but from the USNB, and they were in the street name of FCC. It was Smith who made Coen and FCC aware that these notes were available. Coen did not even make a simple inquiry of the Valley National Bank or Smith who the owner was thereof, despite the many signs pointing to Smith ownership. The only justifiable conclusion is that this failure was deliberate.

All of the foregoing facts and circumstances would be material for disclosure to the public. All that is necessary is that the facts withheld be material in the sense that a reasonable investor might have considered them important in the making of this decision. See Affiliated Ute Citizens v. United States, supra.

A broker-dealer cannot recommend a security unless there is an adequate and reasonable basis for such recommendation. He must disclose the facts which he knows and those which are reasonably ascertainable. By his recommendation, he implies that a reasonable investigation has been made and that his recommendation rests on the conclusions based on such investigation. Where he lacks essential information about a security, he should disclose this, as well as the risks which arise from his lack of information. Hanley v. SEC, 415 F. 2d. 589, 597 (C.A. 2 1969). Coen was deficient in the most elemental compliance with these principles.

The remaining allegations of fraudulent omissions, concerning the failure to advise of the issuance by the Comptroller of the Currency of his Cease and Desist Order and of the resignation by Smith as director and officer of USNB, were not disclosed by the Comptroller until after the $4.2 million worth of notes were sold to the public. Upon learning thereof from an official of this Commission, Coen ceased further sales. While it is true that FCC thereafter made no more than a feeble rescission offer to the last few purchasers, this

is not an element of the fraud charged herein. Finally, the then financial condition of USNB was not publicly revealed, and there is no proof that information of the impact of the fraudulent scheme on its financial condition was known or could have been reasonably discovered.

Accordingly, it is found that Coen willfully (as the term is used in securities laws) violated Sections 17(a) of the Securities Act, Section 10b of the Exchange Act and Rule 10b-5 of the Rules thereunder in omitting to state material facts in connection with the sale of $4.2 million of the subordinated capital notes of USNB between April and June, 1973, by failing to disclose the full circumstances relating to the business practices of USNB, particularly the scheme to inflate its earnings and to make loans of questionable value involving millions of dollars, and that Smith was the actual seller of the securities. The burden of proof has not been sustained by the Division in establishing the other specifications of fraudulent respresentations or omissions.

Any findings under the charge that there was willful violation of the third clause of the fraud sections relating to fraudulent business practices would only reflect what is stated hereinbefore concerning the first two clauses and would merely be redundant. Hence, further findings are unnecessary.

Lack of Supervision over Smither

Finally, the order for proceedings contains a charge that Coen failed reasonably to supervise Smither from 1969 through 1973 with a

view to preventing the commission of the forgery, embezzlement, and other criminal acts for which he was convicted and sentenced to jail, as a person subject to his supervision and who committed such violations (See Section 15(b)(4)(E) of the Exchange Act).

Coen was president of FCC during most of this period. He was an absentee official who spent most of his time in Kansas City, leaving the management of affairs to the employee committees. The criminal acts were committed while Smither was in the Oregon office. He was fired as soon as the facts were discovered.

The Division did not press this issue at the hearing. Moreover, neither in its initial brief nor in its reply brief did it make any reference or request any finding under this charge. Accordingly, it is determined that the Division has waived any finding or conclusion with respect thereto. (Rule 16(d), Rules of Practice).

Public Interest

Respondent Coen having been permanently enjoined from violations of the securities laws, and also having been found willfully to have violated the registration requirements of the Securities Act, to have aided and abetted violations of the financial reporting requirements of the Exchange Act, and to have violated the anti-fraud provisions of the Federal securities laws and rules, all as outlined above, it becomes necessary in the public interest to determine appropriate sanctions to be imposed against him by reason thereof. In so determining, due

regard must be given to the facts and circumstances of each particular case, sanctions being intended not to punish the respondent but to protect the public interest from future harm at his hands. (See Leo Glassman, SEA Rel. No. 11929 (December 16, 1975), at P. 4.)

The Division has urged that only a complete bar from association with a broker-dealer, investment advisor or investment company[26/] would be appropriate. Coen, on the other hand, while not suggesting any particular sanction, urges that limitations on his activities or suspension would be in the public interest, but that a complete bar is not justified.

Coen's position is, basically, that he foolishly placed his trust in Smith and was wholly taken by his scheming and machinations, and that Smith was a widely respected individual by whom many were deceived, even, apparently, governmental authorities. He claims not to have profited from his dealings with Smith, and, in fact, to have lost substantial monies and his reputation as a result thereof. Coen argues that he always attempted to comply with the law and pertinent regulations and instructed those under him to do likewise. He points to a letter of agreement between him and the Commission outlining the manner in which

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26/ The Order makes no charges of violations of the Investment Company or Investment Advisors Acts. In its initial brief, the Division simply asked that Coen be barred from association with a broker-dealer. In its reply brief served to respondents brief, the Division for the first time asks that the bar include "investment advisor or investment company" without any explanation, justification or reference to the facts of record. Consequently, it will be disregarded.

he was to wind up the affairs of FCC as indicative of the faith the Commission placed in him. All accounts of customers of FCC were eventually settled thereunder. Coen has been out of the securities business ever since.

While it is true that Coen was not a party to the basic scheme by Smith to transfer funds of USNB into Westgate and various shell corporations, it is also apparent that there were many signs and surrounding circumstances which reasonably should have put him on notice that greater inquiry and caution were required of him. He had been doing business with Smith for more than twenty years, in a manner presumably satisfactory and profitable to Coen. However, as early as April 16, 1969, there was an article in the Wall Street Journal which attempted to describe how Smith was using his ownership and control of USNB, Westgate, and numerous subsidiaries to engage in transactions profitable to Smith and certain of his relatives and business associates. Coen was named in connection with two transactions. (His claims that he was not made aware of that article at the time it appeared is deemed incredible.) Additionally, there was a private suit brought in 1972 by an individual named Fendler against Coen, Smith and others, alleging a conspiracy. An investigation into all of the activities of these individuals and their associates and affiliates was begun by the Commission in November 1972 in which Coen was made aware of the existence of the related-party transactions by Smith and others. Yet, Coen insists that he first learned of the Smith scheme from a newspaper clipping on September 13, 1975

which was sent to him by someone. Coen puts great reliance on the fact that the Comptroller of the Currency apparently gave Smith somewhat of a clean bill of health by the former's press release on May 31, 1973 followed by a glowing letter of June 12, 1973 from the then president of USNB. This contention is totally irrelevant to the violations found herein since these releases occurred after the events. They could not possibly have affected Coen's actions.

It is unmistakeably clear that Coen deliberately closed his eyes to those signs pointing to the existence of unfavorable aspects to these transactions. When the magic words "real estate investment trust" and tuna fishing "tax shelter" were dangled before him, he permitted himself to be manipulated by Schroeder and Sutter in San Diego, signing whatever papers were sent to him and ignoring the obvious import of the requests for confirmation sent to him by Westgate's auditors. He disregarded ordinary prudence and did whatever he was told. After all, it was through the intercession of Smith and the financing of USNB that he was able to become owner and president of one of the leading broker-dealer organizations on the West Coast. It was through Smith that he was able to unload his non-tradeable Golconda stock for allegedly marketable Westgate stock. When necessary for his own interests, Coen could also act affirmatively (willfully) as when he avoided the registration requirements in the sale of Westgate stock. In the sale of the USNB notes, Coen again demonstrated a conscious effort to avoid the obvious -- that Smith was the owner of the notes. There, he did not

even bother to ask.

The picture that emerges of respondent herein is of a man who, for his own gain, cupidity and profit, would carelessly sign his name to any paper put before him, seek by subtle means to avoid complying with the securities laws, rules and regulations and, at the very least, deliberately disregard the use of ordinary care and business discretion. In either case, or in combination thereof, Coen has not exhibited those qualities of conduct, judgment and trust to be expected of one who as a registered broker-dealer would be dealing with the securities and finances of the investing public. This conclusion is not altered by pro forma instructions to FCC employess to comply with the law, or by the return to FCC customers of their securities and credit balances (but forgetting the millions of dollars of losses suffered by them in Westgate and USNB securities), or by complying with an agreement to wind up FCC affairs according to strict guidelines laid down by the Commission.

Coen's demeanor during the course of the proceedings herein demonstrates a lack of candor and, at times, direct contradictions. During the investigation, when presumably he was not sure how much the Commission knew, he took the position that he was an active participant and fully aware of what was going on, particularly with respect to BCIC (a company actually controlled and manipulated by Smith). During the hearing, when the ramifications of the Smith-Toft scheme, and Coen's

part therein, were bared, Coen claimed he was at times too ill, at other times too trusting, and at still other times too reliant upon Schroeder to know what Smith and his crew were doing. Again, during his oral testimony, he denied on one day that he had any intention of selling his BCIC stock to Smith, but revealed on the next day, after he became concerned over the contents of a newspaper article, that there were serious negotiations including a detailed letter-offer to sell (Fn. 16, above). His testimony as to when he became owner of Elsinor changed from one time to another (Fn. 4, above). In other aspects, his testimony was evasive, obfuscatory, and misleading throughout. For example, he indicates that he became personally obligated on a notes for $620,000 loaned by USNB to finance the purchase of corporate interests by him (Tr. P. 396). He later states that the actual borrower was Dormik (Tr. P. 616). Dormik is a shell corporation. Other examples of this type are too numerous to bear further reference, but support the conclusions concerning Coen's demeanor as a witness, a factor which has been considered in weighing the public interest herein. (See Thomas D. Conrad, Jr., et al., 44 S.E.C. 725, 732, 1971).

The Administrative Law Judge is not unmindful of the fact that during the period involved in these transactions, Coen was confined to the hospital at various times and was operated upon because of a heart condition, that he had invested and lost substantial sums of his own money in FCC and in USNB stock, even shortly prior to the collapse of

the bank, that there are claims against him by the Federal Deposit Insurance Corporation, that he was victimized to a great extent by Smith, and that he has not engaged in the brokerage business since October of 1973. It cannot be overlooked, however, that during the period of winding up of the affairs of FCC, Coen caused FCC to purchase out of its dwindling resources a large block of non-tradeable shares of a company in which he was chairman of the board and his wife stockholder. Moreover, he is still willing to do business with Smith, as witnessed by his recent negotiations to sell the BCIC stock.

From all of the foregoing, Coen's actions have been that of a man who, in his dealings and relationships with others, will act first in his own self-interest over all other interests, sometimes willingly, sometimes carelessly, sometimes recklessly, and sometimes innocently. He will not hesitate to rely upon form and appearance of legality rather than substance, when convenient to do so. Under these circumstances, the likelihood of future misconduct by Coen is sufficient to call for his exclusion from the securities business. Moreover, if remedial proceedings, such as these are to have a truly remedial effect, they must deter not only the particular respondent but also others who may in the future succumb to like temptation (See Arthur Lipper Corporation, SEA Rel. No. 11773 (October 24, 1975) 8 S.E.C. Docket 273, 281). Respondent asserts the doctrine of "suffered enough" in his plea for a

light sanction.[27] However, these are not penal proceedings. The intent is not to punish anyone, but, as stated above, to protect the public interest from future harm.[28]

ORDER

Under all of the circumstances herein, IT IS ORDERED that M. J. Coen be, and hereby is, barred from association with any broker or dealer.

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 (15) 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

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27/ In view of the remedial nature of the proceedings, it should be pointed out that under the Exchange Act and applicable rules, one who is barred from association with a broker-dealer by virtue of an order in a proceeding of this type is not precluded from applying for admission at some future time to re-enter the securities business upon an apprpriate showing. (Abbett Sommer & Co., Inc., et al., 44 SEC 104, Fn. 23, 1969.)

28/ In their proposed findings and conclusions and briefs, the parties have requested the Administrative Law Judge to make findings of fact and have advanced arguments in support of their respective positions other than those heretofore set forth. All such requested findings of fact and conclusions and arguments not specifically discussed herein have been fully considered and the Judge concludes that they are without merit or that further discussion is unnecessary in view of the findings herein.

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.

Jerome K. Soffer
Administrative Law Judge

Washington, D.C.
May 20, 1976