ADMINISTRATIVE PROCEEDING
FILE NO. 3-336

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of	
ARMSTRONG, JONES & CO. (8-6057) THOMAS W. ITIN GEORGE A. REUTER RENE F. CAMPEAU E. KEITH OWENS CHARLES H. BRUCE ROBERT O. SAFFORD	

INITIAL DECISION

Warren E. Blair
Hearing Examiner

Washington, D. C.
February 24, 1967

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Appearances: William D. Goldsberry and Mark A. Loush, of the Detroit Branch Office of the Commission, and Donald W. McKenzie, of the Chicago Regional Office, for the Division of Trading and Markets.

James C. Sargent and Michael Heitner, of Lowenstein, Pitcher, Hotchkiss & Parr, for Armstrong, Jones & Co. and Thomas W. Itin.

James E. Littell and David Robb, of Poole, Warren & Littell, for George A. Reuter.

Harry A. Carson and Thomas A. Roach, of McClintock, Fulton, Donovan & Waterman, for Rene F. Campeau.

W. McNeil Kennedy, Herbert S. Wander, and Michael Warner, of Pope, Ballard, Uriell, Kennedy, Shepard & Fowle, for E. Keith Owens, Charles H. Bruce, and Robert O. Safford.

Before: Warren E. Blair, Hearing Examiner

These proceedings were instituted by an order of the Commission dated October 14, 1965, pursuant to Sections 15(b), 15A, and 19(a)(3) of the Securities Exchange Act of 1934 ("Exchange Act") to determine whether respondents, singly and in concert, wilfully violated and wilfully aided and abetted violations of the Securities Act of 1933 ("Securities Act") and the Exchange Act and rules thereunder as alleged by the Division of Trading and Markets ("Division"), and whether remedial action pursuant to Sections 15(b), 15A, and 19(a)(3) of the Exchange Act is necessary.

The Division alleged, in substance, that in offering, selling, and effecting transactions in the common stock of Alexander Hamilton Life Insurance Company ("Hamilton Life") during the period from November, 1963 to August 31, 1964 the respondents wilfully violated and wilfully aided and abetted violations of Sections 5(a) and (c), and 17(a) of the Securities Act and Sections 10(b) and 15(c)(1) of the Exchange Act and Rules 10b-5, 10b-6, 15c1-2, and 15c1-5 thereunder[1/] by certain conduct and by making and causing to be made untrue statements and omitting statements of material facts concerning that conduct, and concerning Hamilton Life and its stock. Allegedly, respondents obtained control of registrant in the latter part of 1963,

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1/ The Division having failed to pursue its charge of violation of Rule 10b-6 in its proposed findings and conclusions, no further consideration will be given to that alleged violation; that charge is hereby dismissed.

incorporated Hamilton Life in the State of Michigan in October, 1963, and, in the course of a public offering by Hamilton Life of its common stock during the period from November, 1963 to on or about April 20, 1964, sold 2,182,000 shares of Hamilton Life stock which had not been registered under the Securities Act to residents and non-residents of Michigan. Following completion of the public offering, respondents allegedly offered and sold, and bid for and purchased Hamilton Life stock while dominating, controlling, and manipulating its market price by means of transactions which arbitrarily and artificially influenced that price and created a false and misleading impression of the market for Hamilton Life stock. The alleged misrepresentations and omissions concerned the existing and prospective market price of Hamilton Life stock, the amount of insurance in force issued by Hamilton Life, the common control of Hamilton Life and registrant, and the domination, control, and manipulation of the market for and market price of Hamilton Life stock.

The Division further charged that in the offer and sale of stock of Windsor Raceway Holdings, Limited ("Windsor Raceway"), respondents, singly and in concert, wilfully violated, and wilfully aided and abetted violations of Section 17(a) of the Securities Act and Sections 10(b), 15(c)(1), and 17(a) of the Exchange

Act and Rules 10b-5, 15c1-2, and 17a-3 thereunder[2/] by sending confirmations of purchase of, and telegrams seeking payments for, unordered Windsor Raceway stock, and by making entries relating to such purported transactions in registrant's books and records.

General denials of the alleged misconduct or assertions of lack of sufficient information to admit or deny those allegations were filed on behalf of respondents. All respondents appeared through counsel who participated throughout the hearing.

As part of the post-hearing procedures, successive filings of proposed findings, conclusions, and supporting briefs were specified. Timely filings thereof were made by the parties to these proceedings.

The findings and conclusions herein are based upon the record and upon observation of the various witnesses.

Respondents

Armstrong Jones and Company ("registrant"), under its present name and previous styles of Armstrong, Jones, Lawson & White, Inc. and of Charles P. White Company, has been registered under the Exchange Act as a broker-dealer since August, 1957. It is a member of the National Association of Securities Dealers, Inc.,

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2/ The Division no longer contends that Campeau, Owens, Bruce, or Safford participated in or aided and abetted violations involving the Windsor Raceway offering.

and a member firm of the Detroit Stock Exchange.

Thomas W. Itin has been a director of registrant since September, 1963 and also became its president at that time. George A. Reuter, a director and vice-president of registrant since at least August, 1962, has had continuous and direct responsibility for registrant's trading department since that time. Rene F. Campeau was registrant's executive vice-president in charge of sales from January, 1964 until on or about January 4, 1965 and was a director from approximately December 7, 1964 to January 4, 1965.

E. Keith Owens was one of the promoters of Hamilton Life and has been chairman of its board of directors since its incorporation on October 31, 1963 under the laws of Michigan; he has not been associated with registrant itself in any official capacity. Charles H. Bruce, president and a director of Hamilton Life since its inception, was a director of registrant from September 24, 1963 to December 7, 1964. Robert O. Safford, vice-president and director of Hamilton Life since its inception, was also a director of registrant during the period that Bruce served in the same capacity.

Hamilton Life

Hamilton Life, a Michigan corporation, was incorporated on October 31, 1963 for the purpose of engaging in business as

an insurance company. Owens conceived the idea of forming Hamilton Life and with Bruce, Safford, and another associate, James H. Milby, carried that idea through to reality.

Funds with which to commence operations were obtained by an offering of Hamilton Life stock made under a claimed exemption from the registration provisions of the Securities Act available for intrastate offerings.[3/] Initially, the offering by Hamilton covered 1,500,000 shares of Class A stock and 920,000 shares of Class B stock, with the Class A stock being offered to the public at $4 per share.[4/] Mid-Western Investment Corporation, an intrastate broker-dealer formed for the purpose of distributing Hamilton Life stock and wholly owned by Owens, was named as underwriter, and registrant and another Detroit securities firm, F. J. Winckler Co., composed the selling group. The Class B shares, which under certain conditions became convertible and eventually were converted into Class A shares on a basis of one Class A share for 2-1/2 Class B shares, were not offered publicly, but subscribed for at a price of $1 per share by Alexander Hamilton Corporation ("Hamilton Corp.") for whom Owens, Bruce, and Safford also acted as officers and directors.

3/ Section 3(a)(11), 15 U.S.C. 77c(a)(11).

4/ No registration statement with respect to the securities of Hamilton Life was ever filed pursuant to the Securities Act.

The offering of Class A shares commenced on or about November 14, 1963, and met with no marked enthusiasm until about March 1, 1964 when subscriptions began to be received at a rate that the underwriter could not process. On March 23, 1964 the offering was terminated by Owens in order to determine the extent of the subscriptions; a few days later, the offering was found to have been oversubscribed by 682,000 shares. After consultation with the Michigan Securities Commission, offers of rescission were made to subscribers which resulted in rescission of subscriptions to approximately 25,000 shares that were then resold to persons associated with Hamilton Life. Trading of Hamilton Life stock in the over-the-counter market began on April 27, 1964 with the first sale by registrant to a retail customer being for 100 shares at 7-1/2.

Hamilton Life received its certificate of authority to do business on April 30, 1964 and began offering life insurance to the public on May 5, 1964. During the first month, nearly $15,400,000 worth of permanent life insurance was written by the company, and by the end of 1964, there was $60,000,000 of insurance in force which increased to $138,000,000 as of December 31, 1965. An operating loss of about $81,000 was incurred by Hamilton Life during its first eight months ending December 31, 1964, and a further loss of about $280,000 during the year 1965.

"Common Control" of Registrant and Hamilton Life, and Respondents' Concert of Action

Owens first gave thought in 1960 or 1961 to the formation of the insurance company that eventually became Hamilton Life because of his dissatisfaction with the operations of Land of Lincoln Life Insurance Company, for whom he was acting as a regional sales director in Peoria, Illinois. Milby, who was treasurer and a director of Land of Lincoln, joined with Owens in attempts to bring about changes they wanted in that company, and failing that they started to give consideration to a new insurance company. In 1962, Owens met Safford, then connected with sales training in a company which was marketing its products by the door-to-door sales method. Safford became interested in Owens' projected insurance company, and with Owens spent considerable time in formulating plans for its creation. During this planning stage, Safford shifted his employment to that of sales agent for Land of Lincoln and before leaving became another one of its Illinois regional sales directors. After Safford's commitment to the project, Owens approached Bruce, then a vice-president with Illinois Mid-Continent Life Insurance Co., and persuaded him to become the fourth member of the nucleus. As a result of conversations, initially with Safford, and later with Owens and Bruce, Itin associated himself with the group about August, 1962 with the understanding that he was to be one of the regional sales directors of Hamilton Life.

In June, 1962 plans for the formation of Hamilton Life were reduced to writing and supplemented by minutes of meetings held by the group thereafter. Statistical studies of the insurance field caused the group to select Michigan as the best state in which to form their company, and beginning in August, 1962 members of the group moved to Michigan to locate office space, recruit personnel, resolve legal problems, and perform other necessary spade work essential to putting a new insurance company into operation.

Itin moved to Michigan in February, 1963 and anticipating that Hamilton Life would soon receive its Michigan charter, rented an office in Grosse Pointe for his agency operations.

About June or July, 1963 while the group was still waiting for Hamilton Life's charter to be issued, Itin asked Owens, Safford,and Bruce to join with him in the purchase of a controlling interest in registrant. They were agreeable to this proposition and Itin, by September, 1963, acquired between 75% and 80% of registrant's stock for the benefit of the group. On September 24, 1963 Bruce, Safford, and Itin became three of registrant's seven directors and Itin at the same time became registrant's president. When registrant's board of directors was reduced to five on October 16, 1963, they became the majority of the board with Itin serving as chairman. Reuter and Charles A. Dean, registrant's attorney, filled the other two seats. Owens intended to become

a director of registrant, but because of a problem necessitating rescission of sales he had made in Illinois of stock of another insurance company, did not become so associated with registrant. However, Owens was present at some of registrant's directors' meetings, and a confidential "Weekly Management Report" prepared by Itin covering significant aspects of registrant's operations was furnished to Owens by Itin continuously from January, 1964 to at least July 31, 1964.

When Hamilton Life received its charter at the end of October, 1963,Owens, Bruce, Safford, and Itin gave immediate consideration to finding a new president for registrant so that Itin would be able to devote full attention to his contemplated Grosse Pointe insurance agency. The group's unsuccessful search for a suitable replacement made Itin decide, sometime around the first part of 1964, to give up the Grosse Pointe agency and remain with registrant. Following that decision, the group realigned the respective investments in registrant under an agreement whereby Owens, Bruce, and Safford sold their stock interests in registrant to Itin. The agreement provided that Itin would give each of the former a personal six per cent promissory note corresponding to the amount of each one's investment in registrant's stock, and further that registrant would pay monthly to each of them, including Itin, a sum equal to $100 plus 1% of the amount of their

respective stock investments. The latter amount was paid by registrant by means of payments of $850 per month from March, 1964 through September, 1964 to Mid-Western Organizational Consultants, Inc., a Michigan corporation formed in April, 1964 whose stock was owned equally by Owens, Bruce, Safford, and Itin.

Mid-Western Organizational Consultants was conceived as a vehicle through which income derived from any "deal" worked on or in regard to which consulting help was given by Owens, Bruce, Safford, and Itin would be funneled and divided amongst the four. Although not incorporated until April, 1964 Mid-Western Organizational Consultants or a similar organization was in the minds and plans of Owens, Bruce, Safford, and Itin as early as October, 1963 when registrant, by action of its board of directors in which Itin, Bruce, and Safford participated as a majority of the five directors present, voted to retain the consulting services of "Mid-Western Consultants." Besides payments from registrant, Mid-Western Organizational Consultants received "consulting fees" during 1964 from Hamilton Life representing the "override" Itin was entitled to in connection with the sale of Hamilton Life shares sold through registrant during the public offering, and from National Retirement Life Insurance Company in payment of Owens' consulting assistance

relating to an offering of its stock in which registrant participated. Another part that Mid-Western Organizational Consultants played in the Hamilton Life offering took place shortly after March 23, 1964 when Itin brought up the subject of changing the distribution of the underwriting commissions attributable to sales of the oversubscribed stock.[5/] Itin's proposal that as to the oversubscribed stock Mid-Western Organizational Consultants be given the percentage of the commissions which had been allocated to Mid-Western Investment, Bruce, Safford, and Milby on the initially offered shares, was rejected by Mid-Western Organizational Consultants by a three to one vote, Itin being outvoted by Owens, Bruce, and Safford.

The record establishes beyond peradventure that Owens, as the dominant person, with Bruce, Safford, and Milby as close associates, controlled the policies and operations of Hamilton Life throughout the period in question. Owens, Bruce, and Safford, in company with Itin and Reuter, also appear to have controlled registrant during the period in question relating to the public offering of and trading in Hamilton Life stock. Although not associated in an official capacity with registrant, Owens displayed an interest in registrant's operations and

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5/ The 15% underwriting commission on the original offering of 1,500,000 shares was divided on the basis of 8% to the selling agent; 4% to the underwriter, Mid-Western Investment; and 1% each to Bruce, Safford, and Milby.

received consideration and treatment from Itin over and beyond that which could be expected if Owens were merely a creditor of Itin and registrant. Moreover, from September, 1963, when Owens contributed $16,600, over 35% of the amount used by Itin to purchase registrant's stock, until early 1964, when his interest was converted to that of a creditor, Owens was at least a beneficial owner of 25% of registrant's stock. Owens participated in management decisions relating to Itin's compensation as registrant's president and to a possible replacement for him in that position. Bruce and Safford, by their actions as directors of registrant and as associates of Owens and Itin in plans and activities affecting registrant before, after, and during their tenure as directors of registrant, likewise demonstrated that they, with Owens and Itin, were in control of registrant. By virtue of their interlocking directorates for the period in which Bruce and Safford acted as directors of both Hamilton Life and registrant, and of the control found to have been possessed and exercised by Owens, Bruce, and Safford over Hamilton Life and registrant, it is further found that Hamilton Life and registrant were under "common control" during the period relevant to this matter.

Respondents agree that the determination of control is basically a factual rather than legal matter, but argue that the facts here cannot lead to a finding of "common control."

Respondents contend that the Division's assertion of "absolute community of interest" of Owens, Bruce, Safford, and Itin is erroneous, that Itin alone controlled registrant, and that he was without controlling influence over Hamilton Life. Although the Division's conclusion that an "absolute community of interest" existed in these four respondents is too encompassing, the facts do reflect a substantial identity of business interest among them. Their interests varied only in degree between the companies in which they had those interests and revolved around the talents each of the four could respectively contribute to the advancement of Hamilton Life and registrant and to the accomplishment of the objectives of Mid-West Organizational Consultants. The mutuality of interest, however, is only one of the considerations that enter into the finding of "common control," and standing alone is not decisive. As argued by the respondents, the identity of interest does not establish that Itin was a member of Hamilton Life's control group. But respondents' further contention that Owens, Bruce, and Safford, who were in control of Hamilton Life, did not have a controlling influence on registrant is rejected as contrary to the facts which evidence such influence even though day to day operations were left entirely in Itin's hands. It is because Owens, Bruce, and Safford had a controlling influence over both Hamilton Life

and registrant, and not because Itin had such influence in Hamilton Life, that "common control" is found to have existed during the period in question.

The factual fabric that impels a finding of "common control" of Hamilton Life and registrant also lends itself to the conclusion that respondents acted in concert in connection with the offering, selling, and effecting transactions in Hamilton Life stock during the alleged periods. Further, the similarity of the plans and methods used in the creation, financing and operations of Hamilton Life to those found in connection with previous experiences of the promoters, especially with the Land of Lincoln Life Insurance Co., argues strongly that the alleged activities of the respondents formed steps in an overall plan in which Owens, Bruce, and Safford participated from the beginning and registrant, Itin, Reuter, and Campeau later joined. The use of Hamilton Corporation for the purpose of organizing and investing in Hamilton Life instead of the promoters doing so directly appears to have resulted from the fact that other insurance companies had adopted such indirect method. Mid-Western Investment's function in underwriting the Hamilton Life offering corresponds to that apparently performed by Universal Securities Corporation with which Owens and Milby were associated at the time of the formation of Land of Lincoln, and registrant's place in the scheme was obviously to duplicate

with respect to Hamilton Life stock the role that had been played by Central Illinois Investment Company, a securities firm formed by Owens in Illinois, in making a market for Land of Lincoln stock. The fact that control of registrant was purchased instead of a new securities firm's being brought into existence is not significant in making the comparison. The purchase was undoubtedly advantageous to the group in view of the fact that at the time of the purchase the promoters still hoped for an early charter for Hamilton Life and undoubtedly anticipated the need for a market for its stock shortly thereafter. With registrant in existence, delay involved in bringing a new firm into existence and operation would be avoided.

The evidence does not sustain the allegation that registrant, Itin, and Reuter acted in concert in connection with the offer and sale of Windsor Raceway stock. As noted before, the Division makes no contention that the other respondents participated in that activity.

Sale of Unregistered Hamilton Life Stock

Some thought was given in the planning stage of Hamilton Life to filing a registration statement under the Securities Act to cover the contemplated public offering of Hamilton Life stock. However, the delays encountered in obtaining a charter for

Hamilton Life from Michigan authorities, the further delay anticipated in the registration process under the Securities Act, and the advice of counsel engaged by the promoters in Michigan that Securities Act registration was not necessary if the stock were sold only in Michigan, caused the promoters to decide not to register Hamilton Life's stock under the Securities Act. Further delays caused by the rejection of Hamilton Life's initial filing with the Michigan Insurance Commission resulted in the promoters engaging as new counsel the law firm of Joslyn, Joslyn and Dean, which firm made the filings that became effective during the latter part of 1963.

During the course of the public offering of Hamilton Life stock, numerous inquiries from non-residents of Michigan, including friends and acquaintances seeking to purchase shares at the $4 offering price, were received and handled by Owens and Itin. Invariably the inquiries were answered by a refusal to sell the shares being offered by Hamilton Life to such non-residents. However, Owens further advised non-residents that orders for Hamilton Life stock could be placed with registrant and F. J. Winckler Co. for execution after the public offering had been completed, and Itin, in replying, solicited placement of orders for execution in the trading market. Independent of such inquiries and prior to the completion of the offering, Itin also solicited orders for later execution from non-residents

who had given some indication of interest in Hamilton Life stock, and accepted checks that were payment for the stock to be purchased.

The record discloses that the intrastate exemption from registration under the Securities Act was not available for the Hamilton Life offering because sales of stock were not restricted to residents of Michigan. Although the out-of-state sales were few and involved a comparatively small number of shares of Hamilton Life stock, the consequence insofar as making the intrastate exemption unavailable is unchanged.[6/]

Two of the out-of-state sales occurred when non-residents used Michigan residents as agents and nominees. In one instance, a friend of Itin, E.T.S., and two acquaintances of E.T.S., R.D.R. and R.N., all of whom were Illinois residents, used A.C.U., an uncle of R.D.R. living in Cassopolis, Michigan, to subscribe to 1,000 shares. Payment was in the form of a treasurer's check for $4,000 issued by a Chicago savings and loan association and payable to registrant. Itin returned the check to A.C.U. with a request for a new check payable to the bank acting as escrow agent in connection with

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6/ See Edsco Manufacturing Co., Inc., Securities Act Release No. 4413, p. 4-5 (September 20, 1961); Universal Service Corporation, Inc., 37 S.E.C. 559, 564 (1957).

the offering. On or about March 23, 1964, the terminal date for acceptance of subscriptions, Itin telephoned A.C.U. concerning payment for the 1,000 shares, and was advised by A.C.U. that he did not have the money and would request R.D.R. to send Itin a check for $4,000. A.C.U. then telephoned Chicago and left a message for R.D.R. to telephone Itin. In the telephone conversation that followed between R.D.R. and Itin, the problem of making payment before midnight was solved by Itin's making payment by his personal check upon R.D.R's promise to send a check in repayment on the following morning. When the certificate for 1,000 shares was received in due course by A.C.U., he mailed it to E.T.S., who caused the stock to be transferred about June, 1964 into three certificates of 800, 100, and 100 shares, which represented the respective interests of the three actual purchasers.

The second instance of purchases by non-residents through a resident involved D.E.W., a resident of Indiana who was a friend of Owens. Around January, 1964 D.E.W. discussed with D.L.Y., a Michigan resident, the purchase of Hamilton Life's stock in the latter's name. Thereafter D.L.Y. received a prospectus and five subscription forms from Owens, who mailed this material at D.E.W.'s request. D.L.Y. then returned the five subscriptions, each signed by him, with five checks covering an aggregate purchase of 750 shares of Hamilton Life stock and

payment of $3,000 therefor. These subscriptions in fact represented purchases of 200 shares by D.L.Y., 150 shares by D.E.W., 250 shares by an Indiana investment company of which D.E.W. was a stockholder, 50 shares by D.L.D., an Indiana resident, and 100 shares for M.R., another Indiana resident. The certificate for 750 shares subsequently received by D.L.Y. was mailed to registrant in early June, 1964 with a request that the shares be transferred; the new certificates were to be issued in the names of the real purchasers in the respective indicated amounts. Itin's suspicions were aroused by D.L.Y.'s transfer request, and he asked D.L.Y. for more information about the indicated sales to the named transferees, but Itin did not follow up his letter when D.L.Y. did not answer. The transfers were thereafter effected in accordance with D.L.Y.'s request, and new certificates were issued.

A third out-of-state sale occurred when Owens subscribed to 375 shares of Hamilton Life stock for which he paid with $1,500 entrusted to him for investment by C.M., a resident of Kansas. No trust agreement had been executed between Owens and C.M., but an oral agreement was in effect under which C.M. had given to Owens for investment purposes $1,000 in March, 1963 and $500 on or about April 11, 1964. Pursuant to Owens' requests in May and June, 1964, two certificates (one for 250 shares, the other for 125 shares)

were issued in the names of Owens and C.M. In May, 1965 Owens had these certificates canceled and the shares transferred into C.M's name.

Respondents argue that Owens' subscription to 375 shares for C.M. did not result in a sale to a non-resident of Michigan. Underlying the argument is the theory that where an issuer sells to a trustee, the trustee's residence, not that of the beneficiary, governs the determination of whether the sale was made to a non-resident. The theory appears to have merit, 7/ but has no applicability here where Owens did not act in a manner consistent with the claim that he was a trustee. Owens subscribed for the shares not as a trustee, but in his own name; directed that the shares be issued not in his name as trustee, but in his own name and that of C.M., and later directed that the shares be transferred out of his name and reissued in the name of C.M. alone. At no time did Owens retain the entire legal title to the shares in question, or exercise the powers of a trustee. While C.M. might well have held Owens to the obligations of a "constructive trustee," Owens was not a trustee insofar as Hamilton Life or registrant is concerned. Nor does it appear that Owens intended to do anything more, with respect to his relationship to C.M., than to accommodate

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7/ See I Loss, Securities Regulation, 599-600 (2d ed. 1961).

and assist C.M. in selecting an investment. Certainly there is no evidence that he intended to establish and control a trust estate which could be conceived as a source of local funds which would provide part of the "local financing" contemplated by the intrastate exemption.[8/]

Respondents further contend that any violation of Section 5 arising out of the sales to non-residents in the noted three instances cannot be considered wilful because respondents had been imposed upon by non-residents who used deception to achieve their ends in the first two instances, and in the third one, Owens had acted in good faith as a supposed trustee. The contention is bottomed on the concepts that reasonable care or precaution to avoid sales to non-residents is the standard to be applied in determining whether the intrastate exemption has been destroyed, and that, in any event, a violation is not wilful if the person charged did not know that sales had been made to non-residents. These contentions are rejected as inconsistent with settled law.

The intrastate exemption under Section 3(a)(11) affords an exemption with respect to "securities which are 'a part of an issue offered and sold' only to residents of the state in question."[9/] Since Section 3(a)(11) provides an exemption from the general

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8/ See Securities Act Release No. 4386, July 12, 1961.

9/ Ibid.

requirements for registration, it must be "strictly construed" against the claimant thereof.[10/] The refusal of the courts to widen the availability of intrastate exemption by preserving it in the absence of intent or knowledge regarding non-resident sales was indicated in S.E.C. v. Hillsborough Investment Corp., 173 F. Supp. 86, 88 (D. N.H. 1958), wherein the court observed:

> No reason has been suggested why the broad language of section 3(a)(11) should exempt issues where some allegedly sporadic and unintentional sales have been made to non-residents, provided that the remainder are sold only to residents.

Measured by the rule of "strict construction," the presence or absence of either intent or knowledge with respect to the occurrence of out-of-state sales is immaterial on the question of whether the intrastate exemption has been destroyed. In this view it is clear that even without regard to Owens' purchase for C.M., the two sales to the resident agents of non-residents were sufficient to destroy the intrastate exemption for the Hamilton Life offering.[11/] Moreover, it has been

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10/ See S.E.C. v. Sunbeam Gold Mines Co., 95 F. 2d 699, 701 (9th Cir. 1938); S.E.C. v. Children's Hospital, 214 F. Supp. 883, 888 (D. Ariz. 1963).

11/ Further, even were the destruction of the intrastate exemption dependent upon knowledge of the person claiming the exemption that an out-of-state sale has been made, it appears from the record that the circumstances relating to the sale of 1,000 shares to A.C.U. were sufficient to put Itin on notice that A.C.U. was purchasing those shares for non-residents.

the Commission's consistent view that a single sale to a non-resident sufficed to destroy the exemption for the entire issue.[12/] Harsh as such rule may seem from the standpoint of a person seeking to utilize the intrastate exemption, it is consonant with and advances the philosophy of the Securities Act which is to provide, through registration, for the full and fair disclosure of the character of securities being sold.

The fact that respondents may not have been aware that sales had been made out-of-state or may not have intended to make such sales would also be immaterial on the question of "wilfulness." Whether the violation was wilful depends not upon whether the intrastate exemption was wilfully destroyed but upon whether the acts that constituted the violation were "wilful." Here, the Section 5 violations arise out of the fact that the Hamilton Life stock was offered and sold by use of the mails without a registration statement being on file or in effect. The sales to non-residents, whether or not knowingly made to persons of that status, establish that the intrastate exemption from the provisions of the Securities Act was not available for that offering. Since "wilfulness" for the purposes of this proceeding requires no more than that

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12/ See Professional Investors Inc., 37 S.E.C. 173, 175 (1956); Universal Service Corporation, Inc., supra.

the responsible respondents knew what they were going, [13/] and since those respondents who are here found to have committed the Section 5 violations knew or acted in concert with respondents who knew that unregistered stock was offered and sold, such violations were "wilful."

It is concluded that by reason of the foregoing, registrant, Itin, Campeau, Owens, Bruce, and Safford, singly and in concert, wilfully violated and wilfully aided and abetted violations of Sections 5(a) and 5(c) of the Securities Act. The responsibility of registrant, Itin, and Campeau is derived from their direct participation in the offer and sale of unregistered stock, and from the fact that Itin and Campeau were the agents through whom registrant acted, as well as supervisors over registrant's salesmen. [14/] The acts of registrant also become the acts of Owens, Bruce, and Safford as well as of Itin and Campeau because of their participation in the overall scheme which involved the offer and sale of unregistered stock to finance Hamilton Life. However, neither Bruce nor Safford had duties while associated with registrant nor did they or Owens as part of registrant's "control group" act in a manner that thereby would have made them responsible for

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13/ Hughes v. S.E.C., 174 F. 2d 969, 977 (D.C.Cir. 1949); Churchill Securities Corp., 38 S.E.C. 856, 859 (1959).

14/ Shearson Hamill & Co., Securities Exchange Act Release No. 7743, p. 30 (November 12, 1965); Reynolds & Co., 39 S.E.C. 902, 917 (1960).

violations of Section 5.[15/] Similarly, Reuter's duties did not charge him with responsibility in connection with the Hamilton Life offering, and since he had not yet joined the scheme in which the others were participating, Reuter is found not to have violated Section 5.

The evidence relied upon by the Division is not sufficient for it to maintain its contention that an additional out-of-state distribution took place when a part of the original offering of Hamilton Life was resold by resident subscribers before their shares had "come to rest." The resales appear to have been made with stock obtained by registrant from a number of small subscribers to the original issue and through trades with other brokers who had bought from or were selling for numerous small subscribers. There is no substantial evidence indicating that subscribers did not subscribe with the intent to hold their shares for investment or that respondents sold or attempted to sell to persons who did not intend to retain their shares for investment.

The circumstances here are not comparable to those in Lewisohn Copper Corp., 38 S.E.C. 226 (1958), and Ned J.

15/ Cf. Schmidt, Sharp, McCabe & Company, Inc., Securities Exchange Act Release No. 7690, p. 3 (August 30, 1965).

Bowman, 39 S.E.C. 879 (1960), cited by the Division, where initial purchasers who sold to non-residents were found to have purchased for resale rather than for investment. In the Lewisohn case, supra, only about 20% of the allocation to broker-dealers found its way into the hands of customers of those firms. The remainder was put into firm accounts, accounts of members of the firm, and persons closely associated with them, and resold from those accounts within a short period of time. In Ned J. Bowman, supra, a long-time acquaintance of the president of issuer bought 17% of the entire offering and resold almost all of that stock the following month to an out-of-state broker-dealer who in turn sold to non-resident investors.

A serious question is always raised, as the Division points out, concerning whether all of an issue has "come to rest" where, as here, trading begins before stock has even been issued to the original subscriber, and where orders have been solicited from non-residents.[16/] But there must be more than the doubt or inference[17/] raised by the Division in order to rebut the evidence that respondents educed. They have shown that the subscription forms required a subscriber to

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16/ See Securities Act Release No. 4386 (1961).

17/ See Securities Act Release No. 4434, p. 3 (1961).

state that he was purchasing for investment; that the offering was sold in small blocks, except to certain persons closely associated with Hamilton Life who did not resell during the period in question; and, as noted, that the Hamilton Life stock that registrant sold to non-residents after trading commenced came from small subscribers or in the course of trading with other brokers. Under the circumstances, it is concluded that the original offering of Hamilton Life stock had "come to rest" prior to the commencement of trading. This conclusion, of course, in no way affects the previous finding that within the meaning of the Securities Act, sales to non-residents were made by Itin and by Owens during the course of the original offering.

Fraud in Offer and Sale of Hamilton Life Stock

Price Predictions

The testimony of numerous investors who were customers of Campeau or of registrant's various salesmen establishes a pervasive use of unwarranted predictions of rapid and extraordinary price rises as a means to induce purchases of Hamilton Life stock. The contrary testimony of Campeau and of the salesmen, who testified that their customers were not told of such prospective price increases, is not credited in light of the disinterested character of the investors' testimony, the demeanor of the witnesses, the repeated use of such price

predictions by numerous salesmen of registrant, and the likelihood that Campeau infused into registrant's sales force his own practice of making extravagant price predictions.

Campeau told one of his customers that Hamilton Life would "possibly hit 30 or so in four or five years" and that he thought it had "extreme growth possibilities." A second customer of his who bought in June, 1964, was told that Hamilton Life stock looked so good "it might go to $50 a share" by the end of the year, and a third customer was informed with respect to Hamilton Life stock that "this will be a $50 stock in eighteen months."

Richard Zdziebko, then a salesman and now registrant's vice-president, represented to a customer that Hamilton Life was a young, growing company whose stock could appreciate to "around $30" within a year or two, and to another customer that the stock "would go up because it was a good stock," and that it was good investment on which he could make some money.

Seven other of registrant's salesmen, Armstrong, Beals, Pike, Poirier, Rabedeau, Mrs. Terio, and Wadsten, used representations of a similar character in the offer and sale of Hamilton Life stock. One customer of Armstrong testified that in June, 1964 Armstrong had said that he thought it was a good stock because it had risen from $4 to $20 per share and

that in his opinion "it might go to $40 a share," and another customer recalled that Armstrong had said, at a time when the market price was 19½, that the stock could "very easily go to $30." In May, 1964 Beals expressed his opinion to a customer that "the stock would go to $30 or $40" within no longer period than a year. Pike urged a customer to sell other insurance stock and reinvest in Hamilton Life stock at a price of 16 or 17 because he felt it would rise to 23 or 25 within a short period. The next day Pike called his customer to advise him that he could not purchase at 16 or 17 but recommended purchasing at a higher price because he still felt the price would rise shortly. The customer then agreed to purchase, buying 210 shares at 19.

Poirer persuaded a customer to purchase Hamilton Life stock by saying that it was "a good buy" at the quoted price, that there was a "great demand for this particular stock," and that he "didn't know what the price would be the next day or the next week," the latter statement carrying the implication in context of the conversation that the price would possibly be up as quickly as the next day or week. Rabedeau informed one of his customers who purchased on June 8, 1964 that Hamilton Life stock was "very speculative," could "go way down, but also go way up," and that he "definitely expected

it would go up around $30 by the first of the year." Rabedeau induced another customer to buy on June 18 at a price of 19½ by saying that "they had bets on in the office that it [Hamilton Life stock] would go to 27 by the 4th of July." In discussing Hamilton Life stock over the telephone with a customer who placed an order during the conversation, Mrs. Terio stated that "some people had said it would go to $50 a share" and, in effect, that she couldn't see how the company could miss. Wadsten's customer was induced to purchase Hamilton Life stock on June 18, 1964 at 19½ by Wadsten's representing that the price of the stock had multiplied fast and voicing his opinion that he didn't expect it to continue to rise at the previous rate but expected it would at least "double or more than double in a year or two."

The representations concerning a prospective price rise which were used by Campeau and registrant's salesmen in offering and selling Hamilton Life stock were fraudulent and misleading. The Commission has frequently inveighed against projections of price rises to occur within relatively brief periods of time, holding that "predictions of specific and substantial increases in the price of the speculative security are inherently fraudulent."[18/] There can be no

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18/ Floyd Earl O'Gorman, Securities Exchange Act Release No. 7959, p. 3 (September 22, 1966); Crow, Brourman & Chatkin, Inc., Securities Exchange Act Release No. 7839, p. 6 (March 15, 1966); Alexander Reid & Co., Inc., 40 S.E.C. 986, 991 (1962).

question that during 1964 Hamilton Life stock was speculative; it was a new insurance company in a highly competitive field with no history of earnings nor any expectation of earnings in its first few years of operation. True, there was apparent initial success in its insurance sales efforts, but whether such success would continue, and, if so, whether costs could be controlled and management was of such caliber as to assure profitable operation were sheer conjectures. The previous market action of Hamilton Life stock certainly was not warrant for predicting further increases.[19/]

Respondents assert that the price predictions that the Commission has condemned have to be considered in context of the cases in which the Commission expressed its views, that the condemnation be limited to "boiler-room" situations, and that the price prediction must be shown to have been designed at least to induce purchases. Respondents distinguish the present facts from those of previous cases relating to price predictions on the basis that here a majority of the purchasers initiated the purchases, that many were either established customers of registrant or long-time friends of the salesmen, that there was no unfavorable news about Hamilton Life, that registrant's salesmen

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19/ Cf. Crow, Brourman & Chatkin, Inc., supra, at 6 n. 11 of cited release.

were familiar with Hamilton Life's plan and operations, that Hamilton Life stock was represented to be speculative, and that the price predictions at most were mere expressions of opinion. Not one of these distinctions is sufficient to justify the price predictions used by registrant's salesmen.

Although many of the cases involving price predictions that have come before the Commission have involved "boiler-room" sales practices, and others included additional misrepresentations in effecting the sales therein considered, there appears no basis for limiting the proscription against price predictions in the fashion sought by respondents. On the contrary, there is every reason to keep price predictions to a minimum. Probably no representation or inducement held out to a prospective investor could have a greater impact upon his decision to purchase than that of a price rise, for most certainly the risks of loss and the prospects of profit are of paramount importance to him. The customer relies upon the securities salesman, supposedly trained and knowledgeable regarding the "intricate merchandise" he is offering. If a prediction is ventured, even though framed as an opinion, the customer is entitled to assume that the salesman has enough information about the company and its security to support such prediction or opinion, and this

without regard to whether it concerns the future price of the stock or some other aspect of the company or its securities. Where that basis is lacking, price predictions become fraudulent just as any other representations do when made without justification, and are every bit as fraudulent standing alone as when made in conjunction with other misrepresentations. Coupling such predictions with references to the speculative nature of the security tends to whet rather than dampen the interest of the customer, for he is thereby impressed with the fact that the price action of the security can be volatile. Relying upon the salesman, he believes that any price change will be upward. Moreover, the registrant, though not shown to be a "boiler-room," employed salesman who utilized sales techniques, including price predictions, favored in a "boiler-room" operation.[20/] At least in certain instances a customer's investment needs were ignored, financial information regarding Hamilton Life not given, sales of other stock to obtain funds to buy Hamilton Life encouraged, and hasty decisions induced by reference to the unusual market activity in Hamilton Life. Nor does the fact that purchasers of Hamilton Life stock initiated the transaction or were long-time friends of salesmen

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20/ See, e.g., Hamilton Waters & Co., Inc., Securities Exchange Act Release No. 7725 (October 18, 1965).

make the objectionable price predictions more acceptable. An investor is entitled to fair-dealing at the hands of a broker regardless of whether he is the one to make inquiry about a particular stock or is solicited by the broker. And, if anything, a salesman owes a higher duty to a "long-time friend" than to a stranger, for the former may be expected to repose trust and confidence in the recommendations of the salesman whereas the latter would be inclined to exercise a more independent judgment.

The absence of unfavorable news concerning Hamilton Life, relied upon by respondents as a factor that distinguishes the present case from previous decisions involving price predictions, does not help the respondents. Even absent unfavorable developments, the information available to registrant's salesmen regarding Hamilton Life was insufficient to warrant their extravagent predictions.

Failure to Disclose Common Control

Since common control of Hamilton Life and of registrant existed while registrant was effecting transactions in Hamilton Life stock with customers, registrant was required by Rule 15c1-5 under the Exchange Act to make disclosure of such control "before entering into any contract with or for such customer

for the purchase or sale of such security."[21/] The uncontradicted testimony of investor-witnesses is that at the time they made their purchases of Hamilton Life stock no disclosure of such common control was made to them by registrant's salesmen. Respondents, however, contend that a disclosure of registrant's relationship to Hamilton Life sufficient to comply with Rule 15c1-5 may be found in the confirmations used by registrant in connection with its Hamilton Life transactions.

The confirmations in question do not have the disclosure respondents claim for them. The only indication that registrant was under common control with Hamilton Life is found in a printed legend on the reverse side of the confirmations stating, "an officer of this corporation [registrant] is a director of the issuer of the security hereon." A code number on the face of the confirmation is used as a reference to that legend. Respondents concede that the legend is inaccurate in that, in fact, two officers and directors of the issuer were directors of registrant during the period in question.

Respondents misconceive the disclosure required when they view a factually inaccurate reference to a common relationship between registrant and Hamilton Life as coming within the

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21/ Rule 15c1-5 includes as a "manipulative, deceptive, or other fraudulent device or contrivance" within the meaning of Section 15(c)(1) of the Exchange Act the failure of a broker or dealer to disclose to a customer that it is in a control relationship with the issuer whose securities are involved in the transaction to be effected with such customer or for his account.

intendment of Rule 15c1-5. Not only did the recipient of such information not have notice of the common control through a statement by registrant to that effect, he was misled regarding the nature of the relationship actually existing and deprived of facts that would enable him to form his own conclusions.[22/]

Domination, Control, and Manipulation of Market for Hamilton Life Stock

When approval for registrant to commence trading in Hamilton Life stock was not forthcoming from the Michigan Securities Commission by April 27, 1964, Itin telephoned officials of that agency. In the conversation, Itin spoke of "the pressure of interest from both within the State of Michigan and outside the State of Michigan,"[23/] and asked if registrant could begin trading. When one of the officials demurred to the commencement of trading before the stock had been physically issued, Itin suggested that registrant be permitted to trade on a "when, as, and if issued" basis. Registrant was then given permission to trade Hamilton Life stock on that basis, but upon condition that until April 30, 1964 only unsolicited buy and sell orders were to be executed.

22/ See III Loss, Securities Regulation, 1479 (2d ed. 1961).

23/ Registrant, according to Itin, had a "pile of buy tickets" and three sell tickets. In addition, inquiries about the commencement of trading had been received.

Itin immediately informed Reuter that trading could commence, and Reuter reacted by going down his keyboard, which had direct telephone connections with fifteen to eighteen broker-dealers, and asking each of those securities firms whether it had buy or sell orders on Hamilton Life stock. In every instance Reuter received a negative reply. When Itin appeared in the trading room about fifteen minutes later with a sheaf of orders that had been placed with registrant for execution when the market opened, Reuter told him of the lack of interest by other firms. Itin's resolution of the impasse caused by the absence of professional interest was to open the market by crossing orders placed with registrant, selling 100 shares to a customer at 7½, and, eleven minutes later, according to the time stamp, purchasing 100 shares from another customer at 7. Itin then told Reuter, who was sitting across the desk from him, that the market was 7-7½. Reuter, in turn, called several brokers, telling them that the market had opened at 7, and asking if they had any stock. When one broker asked 7½ for 1,000 shares, Reuter consulted Itin and obtained approval of the purchase. For the first three days, trading in Hamilton Life stock was so heavy that Reuter asked for and received assistance in the trading room from Itin and Campeau. Itin executed all of the purchase orders received by registrant from its customers, Reuter did the trading with other

brokers, and Campeau kept the record on registrant's position in Hamilton Life stock. During this initial period, when trading was on a "when, as, and if" basis, registrant's purchases from other brokers of 24,150 shares accounted for about 75% of the total shares purchased in the wholesale market. In these same three days registrant sold a mere 795 shares of Hamilton Life in the wholesale market while selling nearly 25,000 shares to its retail customers. The majority of the shares were sold to Itin's own customers, some of whom had indicated their interest prior to the commencement of trading. Prices to registrant's retail customers during this period ranged from 7½ to 9 7/8, with the price rising over the preceding retail price fifteen times in the first two days.

Registrant's purchases of nearly 174,000 shares from other broker-dealers in Michigan during the entire period of April 27, 1964 through August 31, 1964 represented over 60% of all purchases in the wholesale market. The sales by registrant to other broker-dealers during the same period aggregated only slightly more than 34,000 shares. During the same time registrant accounted for over 70% of all retail sales by selling 224,104 shares to its customers.

Registrant first appeared in the sheets on April 29, 1964, the only broker that day. Its bid of 7 3/4 and ask of 8 1/4 on Hamilton Life stock increased by 1/2 both the bid and

ask of the initial quotations of 7¼ - 7 3/4 placed in the previous day's sheets by W. B. Wolf & Co. of Detroit. On April 30 registrant, again the only broker in the sheets, raised its quotes by 1½ to 9 1/4 bid, 9 3/4 asked.

During the entire period in question, April 27 through August 31, 1964, which encompassed 89 trading days, registrant appeared in the "pink" or "green" sheets 24/ or both 84 times, placing bid and ask quotations in 82 of these instances. Of five other brokers also appearing in the sheets during the same period, W. B. Wolf & Co. was in 48 times; Smith, Hague & Co., 25 times; F. W. Winckler Co., 12 times; C. N. Davidson & Co. placed ask prices on two days; and Wm. C. Roney placed ask prices on three days. On 33 days, registrant was the only broker placing a bid and ask price in the sheets, and it raised its bid on fifteen of those days, lowered the bid on ten, and kept its bid the same on the remaining eight days. Of the 49 days on which other brokers accompanied registrant in the sheets, registrant had the high bid on 30 days, shared the high bid on 10 days, and had a bid lower on nine occasions.

Registrant's trading in Hamilton Life stock during the entire period also evidences an intent to raise the market

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24/ The color of the paper on which the National Daily Quotation Bureau, Inc. publishes its Eastern Section is pink; that for the Western Section is green.

price of that stock and to keep the level of the market on a higher plane than dictated by normal interplay of buyers and sellers in an open market. In addition to the predominant purchases on the wholesale market and sales of that acquired stock to retail customers having the effect of drying up the floating supply of the stock, registrant maintained price leadership in the actual day to day trading in the stock amongst brokers in Michigan. In buying Hamilton Life stock from other brokers, registrant in 187 instances raised its price over the immediately preceding price paid by any broker in the wholesale market, compared to the next highest broker-dealer who had 44 raises and to the remaining 50 brokers-dealers trading during the period of whom only eleven raised their prices on the inside market as many as ten times. With respect to its customers, registrant in 264 instances upped the sales price over that which immediately preceded in the retail market. All other brokers accounted for a total of 12 similar raises.

Significantly, on each of the 22 trading days in June, 1964 registrant appeared alone in the quotation sheets, 20 times in the "pink," and 20 times in the "green." Registrant's bids were raised on eleven days, were the same as its preceding bid on four days, and were lowered on seven. During June, registrant bought over 53,000 shares of Hamilton Life stock

from other broker-dealers, thereby accounting for over 75% of the purchases in the wholesale market, while it was selling more than 77,000 shares to retail customers, an amount equal to nearly 85% of the total shares sold in the retail market in June. During this month, registrant had a short position on four days, June 2 to 5 inclusive, and a long position of over 300 shares at the close of each of the remaining eighteen trading days. Registrant's selling price to its customers ranged from 11½ on June 1 to a high of 20½ charged on June 19.

The surge in the prices during this brief period is marked in particular by a 4 point rise in the five day trading period of June 15 - 19. During that period registrant's inventory of Hamilton Life stock climbed from 388 shares to 1,888 shares at the close of June 19, reaching an interim high of 3,507 shares on June 18. After June 19 and for the rest of the month, registrant's prices to its customers and in the sheets declined, apparently because registrant's position in Hamilton Life stock was getting too long for Itin's liking. Itin's own testimony was that about June 20, and over a period of six or seven trading days to July 1, registrant "walked the stock [Hamilton Life] back down" from 20 to 12 when its position began getting long. Itin also testified that on July 1 there was an hour or so during the trading day that the stock dropped

from 15 or 16 to 11 or 12 while registrant had a "work-out" market.[25/] During the five trading days following July 2 when W. B. Wolf & Co. inserted a bid of 10¼, the bids in the "pink" sheets were successively higher each day, registrant being the high bidder three times, including the fifth day when its bid was 15.

The actions of Hamilton Life in placing newspaper advertisements of an extremely self-laudatory nature on April 22 and June 16, 1964 are also a material consideration on the issue of manipulation. Although the inaccuracy in the June 16 advertisement, which represented that Hamilton Life had over $15,000,000 of insurance in force when in fact that amount had been written but was not yet "in force," may well have been materially misleading to a knowledgeable investor in insurance stocks, the inaccuracy is not considered to be significant in connection with the question of whether the stock was manipulated. However, even granting respondents' claim that the primary purpose of these advertisements was to generate interest in the insurance policies of Hamilton Life, it is not reasonable under all the circumstances to view them as being without the secondary purpose of stimulating interest of the investing public

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25/ See Tr. 3370-71. A "work-out" market has been described as one in which a trader acts essentially as a broker and attempts to find interest on the other side of the market. Shearson, Hamill & Co., Securities Exchange Act Release No. 7743, p. 12 n. 22 (November 12, 1965).

in the stock of Hamilton Life.

The picture that emerges from the trading pattern and other evidence relevant to registrant's trading and selling activities is of a market for Hamilton Life stock dominated, controlled and manipulated by registrant during the period April 27, 1964 to August 31, 1964. With an eagerness amounting to anxiety, and without ear for the cautionary words of the president of the Detroit Stock Exchange, Itin caused registrant to open the market at a price of his own choosing in the absence of any independent interest, and thereafter caused registrant to be an aggressive leader in the sheets in connection with that market. At no time does it appear that registrant dropped out of the market in order to let the independent forces of the market prevail except upon the brief occasion on July 1, 1964. The results experienced in that instance, a sudden drop of three or four points within an hour or so, is indicative of the control that registrant had imposed upon the market for Hamilton Life stock. Registrant was not only the primary wholesale dealer but also the primary retailer of Hamilton stock. It was upon registrant's ability, through assiduous efforts by its salesman to place stock purchased in the wholesale market, that the market depended. The market created and nurtured by registerant was not subject to the vicissitudes of independent forces of supply and demand, but was a

reflection of the efforts of those in control of registrant to raise and control the prices at which Hamilton Life stock would be traded or sold to the public. It is apparent that registrant published quotations on and effected transactions in Hamilton Life stock at prices that were arbitrary and artificial for the purposes of raising the price level and creating a false and misleading appearance of the trading activity of that security and of its market. Doing so constituted a manipulative scheme and device in violation of the securities acts.[26/]

It is well settled that where a dealer dominates, controls and manipulates the market in the security which it is attempting to sell, it must make full disclosure thereof so that the customer will not be misled into believing that the price to be paid for the security has been reached in a free and open market.[27/] Moreover, such disclosure is essential in order to allow the customer to judge the marketability or liquidity of the security. The failure to disclose registrant's domination, control, and manipulation of the market for Hamilton Life stock was misleading to purchasers of that stock.

26/ Cf. R. L. Emacio & Co., Inc., 35 S.E.C. 191 (1953).

27/ See J. H. Goddard & Co., Inc., Securities Exchange Act Release No. 7618 (June 4, 1965); Bruns, Nordeman & Co., 40 S.E.C. 652, 659 (1961); Sterling Securities Company, 39 S.E.C. 487, 492 (1959); R. L. Emacio & Co., Inc., supra.

Respondents assert that motivation, an important consideration in the cases cited and relied upon by the Division, is missing here and that a "stock manipulation scheme . . . is totally at odds" with respondents' plans for Hamilton Life. The record refutes these assertions, showing not only that respondents' personal fortunes would be enhanced by an increase in the price of Hamilton Life stock, but also that the success of Hamilton Life was largely dependent upon its stock showing market improvement.

As the respondents knew and stated in the Hamilton Life prospectus, the life insurance business is highly competitive, and Hamilton Life's success dependent upon its ability to sell "insurance and administer its affairs." The prospectus expands upon the methods to be used to attract salesmen and administrative personnel by stating: 28/

> . . . Because it is a new venture, the Company [Hamilton Life] has considered it advisable to attract to itself, personnel experienced in the administration and sales of life insurance, and it is contemplated that the agency program through which the insurance is to be sold and the stock option plan will accomplish this.

The purpose of the stock option plan, together with some details of the plan, is again referred to in the prospectus as follows: 29/

28/ Owens Exhibit C., p. 10.

29/ Id. at 7.

> The Company shall adopt an appropriate restricted stock option plan for the purpose of attracting and retaining the services of qualified sales and executive personnel. . . . the option price will be at least 95% of the fair market value at the time the option is granted. 30/
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> The Company will set aside a maximum of 200,000 shares of its Class A Common Stock for stock option purposes. At least 50% of such options shall be allocated to general agents, sales agents, and members of the Resident Advisory Board. 31/ The remaining options shall be allocated to officers, directors and Home Office personnel. These options can be allocated among both present and future personnel. [Footnotes added.]

Underscoring the importance of stock options to Hamilton Life's future are the following references in the prospectus 32/ to the problems of setting up its agency organization:

> . . . It may be difficult for the Company to obtain the services of the older and more established agents in the areas in which it proposes to sell its policies.
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> . . . . . .

30/ Bruce testified that the option price was the price prevailing at the time the option was issued. See Tr. 4491.

31/ The Resident Advisory Board consisted of 100 members in May, 1964 with each member to receive an option for 100 shares at a price of $4, and the right to subscribe for up to 2,000 shares in the Hamilton Life offering. The members, who resided in different communities throughout Michigan, were supposed to assist Hamilton Life in finding sales agents, and to otherwise advance the company's interests in their respective areas.

32/ Owens Exhibit C, p. 11.

> The Company proposes from time to time during its early years of operation to grant non-assignable options to purchase common stock to writing agents and General Agents as production awards. There is no assurance how much incentive said options would provide the Agents, as other companies also provide incentives to have agents select their policies for persons purchasing insurance. [Emphasis supplied.] 33/

The sales commission contract that Hamilton Life offered to prospective sales personnel was "55% to the agent, 70% top to the regional director," and "it was less than almost every new company." 34/ After writing $500,000 of insurance, a sales agent received options at the rate of 20 shares of common stock for every $100,000 of insurance in force.

It would be unrealistic to assume that salesmen with the qualifications looked for by respondents, and especially those with established companies, would drop existing business connections to go with Hamilton Life unless they believed such move would be to their material advantage. Since Hamilton Life elected to offer smaller commission contracts to sales personnel, the stock options had to have enough lure to compensate them for the lower commissions and to induce them to make a shift in their employment or sales efforts. Similarly, the stock options offered to members of the advisory board and

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33/ General agents were called regional directors by Hamilton Life. Owens Exhibit C, p. 11.

34/ Tr. 4491 (Testimony of Bruce).

administrative personnel would have to appear to have value in the near future in order to induce them to associate themselves with Hamilton Life. It was essential that the market price of Hamilton Life show improvement, for if it did not, the personnel upon whom Hamilton Life was completely dependent for success would most naturally refuse Hamilton Life's offers of employment, or if already with Hamilton Life, become dissatisfied with their valueless stock options and soon leave for greener pastures. Respondents therefore had a very real interest in whether the stock options became valuable and in making a market for Hamiiton Life stock and attempting a manipulation of the market price to assure that such value became immediately apparent.

Respondents' view that the "pink" and "green" sheets are valueless in deciding whether a manipulation took place is unacceptable. Even though the sheets are regarded by brokers as nothing more than indications of the market, the sheets still point to the brokers interested in trading in a particular security and its approximate price range. When the same broker or brokers appear in the sheets over a sustained period at increasing prices, the impression created is one of activity in which demand is consistently greater than supply. The question is not, as the respondents indicate, whether the sheets reflect a precise market price at a

given time, which they do not, but whether they portray a price rise over a period of time. Respondents' contention that actual trading by other brokers and their presence in the sheets at prices corresponding to those found in registrant's quotations and trades indicates an absence of manipulation has a serious flaw. It is true that one of the indicia of a free and independent market is the participation in that market by several securities firms, but such participation does not exclude the possibility of manipulation. Here, the other brokers quoting or trading Hamilton Life stock knew that registrant was the primary market maker, were undoubtedly constantly aware of registrant's quotations, and would recognize the potential of a trading profit with little danger of serious loss by evidencing an interest in Hamilton Life stock at or about the price range in which they knew they could sell to registrant.

No substantial error has been found in the schedules introduced by the Division covering the trading in Hamilton Life stock during the relevant period nor in the approaches used in the preparation of those schedules. The schedules of "raises" or up-ticks in price need not take into consideration the fact that prices had been lowered prior to the up-tick taking place nor include agency transactions before becoming acceptable as evidence of registrant's intentions.

The schedules serve, without the additions that respondents insist upon, to show that day after day registrant was aggressive in trading up the price of Hamilton Life stock, excepting only in those periods where registrant's inventory outpaced the ability of registrant's salesmen to retail registrant's purchases. Were the additions made, the appearance of registrant's aggressiveness would yet remain, and it is that aggressiveness in the light of the other evidence adduced which is material and relevant on the issue of manipulation.

Again with respect to registrant's apparent reduction of the "floating supply" of Hamilton Life stock by siphoning it off the wholesale market and into the hands of retail customers, the action is regarded as only one aspect of the trading that must be carefully weighed. Although, as respondents claim, a characteristic of a principal market maker may be the purchase of more shares from dealers than sold to dealers, it is also true, as respondents concede, that such activity is likewise characteristic of the market manipulator. 35/

The other arguments and contentions of respondents on this issue are equally unpersuasive in the face of the convincing evidence that respondents engaged in a manipulation to protect and increase their individual fortunes and that of Hamilton Life.

35/ See, e.g., Barrett & Co., 9 S.E.C. 319, 327-28 (1941); Gob Shops of America, Inc., 39 S.E.C. 92, 102 (1959).

Conclusions

As indicated, Owens, Bruce, and Safford, later joined by registrant, Itin, Reuter, and Campeau, acted in concert in carrying out a plan to launch Hamilton Life in the insurance business and to provide a market for its stock. It is concluded that in connection with that plan and as an integral part of it, fraudulent offers and sales of Hamilton Life stock were effected by means of unwarranted and extravgant price predictions, by failure to disclose the existence of common control over Hamilton Life and registrant, and by failure to disclose the domination, control,and manipulation of the market for Hamilton Life stock. It is further concluded that by reason of the foregoing, respondents, singly and in concert, wilfully violated, and wilfully aided and abetted violations of Section 17(a) of the Securities Act and Sections 10(b) and 15(c)(1) of the Exchange Act and Rules 10b-5 and 15c1-2 thereunder.

Hamilton Life Prospectus

During the course of the hearing, evidence relating to the prospectus used in connection with the Hamilton Life offering was introduced into the record. The Division contends that the prospectus failed to disclose material facts relating to the financing of Hamilton Life, and submits proposed findings to the effect that the failure to disclose

such facts made the prospectus misleading and its use a violation of the anti-fraud provisions of the securities acts. In opposing the Division, respondents argue that the Order for Proceedings did not charge them with the violation which the Division now alleges, and that respondents did not have prior notice of that charge nor time to prepare a defense against it.

The position of the respondents on this question is well-taken. No finding or conclusion on whether a violation of the securities acts took place as a result of the alleged deficiencies in the prospectus would be proper at this time. The Order for Proceedings does not include adequate notice that the Division was charging a violation arising out of the use of a faulty prospectus and if the language of the Order for Proceedings could be strained to imply that a prospectus had been used in the offering of Hamilton Life stock, there would still be no notice of the nature of the alleged deficiencies in that prospectus. It is not enough to charge a violation substantially in the words of a statute when the statute itself does not adequately describe the offense. There must be some defining of the nature and elements of the offense charged to permit respondents to prepare their defense.[36/] As to the Division's point that the Order for

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36/ See Michael J. Meehan, 1 S.E.C. 238 (1935).

Proceedings may be amended pursuant to Rule 6(d) of the Rules of Practice to include the additional charge relating to the prospectus, it suffices to note that no amendment was requested nor authorized during the course of the hearing, and that under Rule 6(d), the power of the hearing officer to authorize amendments to matters of fact and law ceases at the close of the hearing.

The conclusion reached on this question is not to be construed as meaning that the evidence relating to the prospectus is not relevant and material to other issues properly charged in the Order for Proceedings. Quite the contrary, for the testimony has a bearing on the credibility of the witnesses, and the prospectus furnishes, at very least, a further insight into the relationships existing between Owens, Bruce, Safford, and Itin, and the preferential treatment accorded to them by Hamilton Life and Hamilton Corp. Important, too, are the revealing references in the prospectus to Hamilton Life's stock option plan and the need for it.

False Confirmations Relating to Windsor Raceway Stock

A registration statement pursuant to the Securities Act was filed on October 23, 1964 by Windsor Raceway covering a proposed offering of 350,000 units of its Class A and B stocks in units consisting of one share of each class of stock

and naming registrant as the underwriter thereof.[37/] A series of amendments to the registration statement were filed which caused the effective date of the registration statement to be delayed until December 21, 1964.

Commencing on October 23, 1964 registrant's salesmen solicited "indications of interest" in Windsor Raceway stock from prospective investors and continued to do so until early the next month, when the indications received totaled more than the contemplated offering. Upon being advised on December 21, 1964 that the registration statement had become effective, Itin instructed registrant's sales force to call, if possible that day, all persons who had indicated an interest, and to firm up the indication previously given. Itin further informed the sales force that except for persons whose names they were to give to the office that day, everyone who had indicated an interest would be sent a Windsor Raceway prospectus and a confirmation of sale by mail that night. According to Itin, registrant mailed confirmations that evening in accordance with the stated procedure.

Amongst the persons to whom these confirmations of purchase were sent were a large number who had not been called by registrant's salesmen on December 21, and who had never placed

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37/ S.E.C. File No. 2-22868.

an order for Windsor Raceway stock. Mrs. Terio, one of registrant's salesmen, testified that on December 21 she was able to telephone only 25 or 30 of the 150 prospective investors who had previously given her indications of interest. She was unable to recall whether at the end of that day she informed Itin or any of the other supervisory personnel of the extent of her calls. Mrs. Terio's testimony and that of members of the public who either disclaimed giving any indication of interest or stated that only an indication of interest had been given to Mrs. Terio or another of registrant's salesmen, make it clear that registrant mailed confirmations of purchase of Windsor Raceway stock to persons who had not ordered that stock. Some but not all of the purported sales were canceled upon request, depending upon whether such requests were received by registrant on or before January 8, 1965.

Registrant and Itin attempt to equate the "indications of interest" taken in the Windsor Raceway offering with "offers to buy," and argue that registrant was accepting those "offers to buy" when confirmations were sent to persons who had previously given "indications of interest." Neither the authorities upon which they rely nor the facts in the record support their position.

In asserting that an indication of interest is "an euphemism for the taking of 'offers' in the statutory sense,"[38/] respondents misquote their authority, I Loss, Securities Regulation, 215 (2d ed. 1961). The quotation referred to reads correctly, "a euphemism for the making of 'offers' in the statutory sense. . . ." [Emphasis supplied]. The difference is critical, for the correct quote not only fails to support, but refutes, respondents' submitted equation, and substitutes the thought that the solicitation of "indications of interest" should be looked upon as the underwriter's offers to sell. That Loss does not agree with respondents is further indicated by the subsequent suggestions on appropriate conduct during the waiting period found in that treatise, id. at 224:

> Perhaps the safest technique is to solicit offers to buy, which the seller can then accept after the effective date. . . . Or he can simply "offer" in the statutory sense by soliciting "indications of interest" and state that no offer for a contract (in the common law sense) will be made until the effective date.

The excerpt from the case of Franklin, Meyer and Barnett, 37 S.E.C. 47, 50 (1956) used by registrant and Itin in their brief[39/] is of no aid to the respondents, for the instructions given by the partner

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38/ Brief of Respondents Armstrong Jones and Company and Thomas W. Itin, p. 66.

39/ P. 71.

of that registrant to its salesmen included a direction that "indications of interest had to be 'firmed up' before a confirmation of sale could be sent to the customer." If the "indications of interest" were in reality "offers to buy," there would have been no need for the Franklin partner to "firm up" those indications; confirmations could have been sent without that additional step.

That "offers to buy" Windsor Raceway stock were not being taken by registrant's salesmen is also apparent from the credible testimony in the record. The conversations that the salesmen had with prospective investors were not couched in language indicating either that the salesmen were seeking, or that the prospects were giving, "offers to buy." Rather, those conversations reflect the usual and customary solicitation by salesmen of an underwriter that is attempting to test the extent of the interest in its contemplated underwriting. It appears that the present contentions are defenses contrived for use in these proceedings, and that at the time of the solicitations Itin considered the "indications of interest" in no other light than preliminary inquiries.

By sending confirmations of unauthorized transactions in Windsor Raceway stock, registrant represented to the recipient of each confirmation that a sale had taken place based upon the existence of effective orders or authority.[40/]

40/ Shelley, Roberts & Co., 38 S.E.C. 744, 751 (1958).

Inasmuch as the recipients had neither placed an order nor authorized a purchase of Windsor Raceway stock for their accounts, registrant's representation was false and constituted a wilful violation of Section 17(a) f the Securities Act and Sections 10(b) and 15(c)(1) of the Exchange Act and Rules 10b-5 and Rule 15c1-2 thereunder.[41/] In addition, because the use of false confirmations also involves the making of false and fictitious records,[42/] registrant wilfully violated Section 17(a) of the Exchange Act and Rule 17a-3 thereunder.

It is further concluded that Itin by virtue of his responsibility for registrant's conduct and for the conduct of the salesmen under his supervision, wilfully aided and abetted registrant's violations, and wilfully violated Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. Reuter's duties as a director of registrant and as its vice-president were not such as would make him responsible for the violations that occurred in connection with the Windsor Raceway offering. It is concluded that Reuter, as well as Campeau, Owens, Bruce, and Safford who the Division concedes were not involved in this aspect of registrant's operations, did not commit such violations.

41/ R. A. Holman & Co. v. S.E.C., 366 F. 2d 446, 451 (2d Cir. 1966).

42/ Shelley, Roberts & Co., supra.

Due Process

Respondents complain that due process has not been accorded to them in these proceedings as a result of the unfair investigation that preceded the institution of the proceedings, the refusal of the Division to allow respondents to examine prior statements of witnesses until after they had completed their direct testimony at the hearing, and the submission by the Division of distorted Proposed Findings of Fact. None of these complaints has substance.

There is nothing in the record that indicates the Division took an inordinate amount of time to investigate this matter or took undue advantage of those who were interviewed. The time that elapsed from the indicated inception of the Division's investigation to the institution of these proceedings appears quite normal, if not less than might be expected, considering the nature and complexity of the case that grew out of that investigation. Further, none of the matters specified in the respondents' proposed findings and upon which they rely for support of alleged unfairness during the investigation is established to an extent that creates doubt about the due process accorded respondents.

The Division's refusal to furnish the prior statement of a witness before he had completed his direct testimony was

in accord with the so-called Jencks statute,[43/] whose applicability the Commission extended as a matter of policy and practice to its administrative hearings.[44/] It is also noted that the Division made an offer to turn over a witness' statement the night prior to that witness taking the stand upon condition that opposing counsel not communicate with the witness before he took the stand. Counsel for one respondent took advantage of that offer; the others could have. Further, there was no denial of any request for a recess or adjournment to permit examination of such statements before cross-examination. It is assumed that when counsel did proceed with cross-examination, they felt adequately prepared to conduct it. This is not to say that counsel for respondents might not have better prepared for such cross-examination if they had the statements of the witnesses earlier, nor that the hearing might not have been expedited to some extent if the Division had been willing to release the statements in question when first requested to do so. However, the election belonged to the Division, and due process was not impaired by its refusal to accede, except upon condition, to the respondents' request.

43/ 18 U.S.C. §3500 (1957).

44/ Codification of this policy and practice was effected by the adoption on August 2, 1966 of Rule 11.1 of the Rules of Practice.

Respondents' claim that due process was denied to them because of the character of the Proposed Findings of Fact submitted by the Division is nothing more than frivolous. In these proceedings, the Division is an advocate, and it is to be expected that the Division would act in that fashion not only during the hearing, but in connection with the post-hearing procedures. The Proposed Findings of Fact and Conclusions of Law submitted by the Division are entirely proper, and no less so because some of its proposals have been rejected as not being consistent with the findings herein.

Public Interest

In view of the serious and extensive nature of the violations established by the record, the respondents' contentions that sanctions are not appropriate in the public interest must be rejected. However, the mitigative aspects of the circumstances respondents urged have been taken into consideration in assessing the sanctions which need be imposed.

It is concluded that registrant's registration as a broker-dealer should be revoked, that registrant be expelled as a member firm in the Detroit Stock Exchange and from membership in the NASD, and that Itin be barred from association with a broker-dealer. Because it is believed that the public would not be endangered if Itin were allowed to work in a supervised capacity, it would be appropriate to permit him, after one year,

to be employed by a broker-dealer in a supervised capacity. These sanctions, severe as they are, are warranted by Itin's demonstrated lack of concern for his responsibilities to the public in his role as principal of registrant. Under Itin's stewardship, registrant's activities in the original offering and subsequent trading of Hamilton Life stock were devoted primarily to the advancement of his personal interests and those of Owens, Bruce, and Safford. There is an open question as to whether Itin, a newcomer to the securities business, realized the full import of his manipulative activities in the stock of Hamilton Life; if there were not, the bar would be without qualification. Giving Itin the benefit of the doubt does not change the conclusion that Itin over a long period of time showed an inexcusable ineptness or unwillingness to upgrade registrant's operational and sales practices to a level in keeping with the standards required of a broker-dealer. Even if registrant's misconduct were to be attributed solely to Itin's inexperience, the interests of the investing public would still require the indicated sanctions. Although the extent of the injury to investors is not susceptible to precise determination, it was substantial, and occurred when purchasers were forced to pay artificially inflated prices for Hamilton Life stock. The failure to register that stock under the Securities Act deprived investors of material

information concerning Hamilton Life to which they were entitled. Had such information been available, it might well have dampened an investor's enthusiasm for the stock during the offering and thereafter. Further, there is no assurance that the false confirmations sent by registrant did not cause persons who would not have otherwise ordered Windsor Raceway stock to accept that stock and make payments in accordance with registrant's demands.

It is concluded that Reuter should be expelled as a member of the Detroit Stock Exchange and suspended from association with a broker-dealer for a period of six months. Reuter's participation in the fraudulent scheme found herein is aggravated by the fact that he lent his experience and reputation to an illegal enterprise that could not have been placed in operation without his assistance. His previous unblemished record of 35 years in the securities business and the high regard in which he is held by others in the securities industry who have had long acquaintance with him argue strongly and effectively against a sanction greater than that indicated.

It is concluded that Campeau should be barred from association with a broker-dealer with a right, after six months, to apply for permission to re-enter the securities business under adequate supervision. Campeau's conduct, taking into account

his prior experience with his own securities firm, clearly demonstrates his inadequacy as a sales manager or as a principal of a broker-dealer. But serious as his misconduct was, it does not appear under all of the circumstances that the public interest would be in jeopardy if he were permitted to return to the securities business in an adequately supervised position.

It is concluded that Owens should be barred from association with a broker-dealer and that Bruce and Safford each be suspended from association with a broker-dealer for six months. The record reflects the leadership and domination of Owens in the conception and operation of respondents' scheme to promote, finance, and obtain a sales force for Hamilton Life. On the other hand, Bruce and Safford, although by no means mere tools, were basically sales-oriented. They appear to have relied in large part on Owens' judgment in matters affecting Hamilton Life's securities, and did not participate in the day to day operations of registrant. It is also to the credit of Bruce and Safford that their candor on the witness stand was considerably greater than that of Owens. The noted differences justify the disparity of the sanction imposed against Owens as compared to those of Bruce and Safford. 45/

45/ All proposed findings and conclusions submitted by the parties have been considered, as have their contentions. To the extent such proposal and contentions are consistent with this initial decision, they are accepted.

Accordingly, IT IS ORDERED that the registration as a broker-dealer of Armstrong Jones and Company is revoked, and the company is expelled as a member firm of the Detroit Stock Exchange and from membership in the National Association of Securities Dealers, Inc.; that Thomas W. Itin, Rene F. Campeau, and E. Keith Owens are each barred from association with a broker-dealer, except that Thomas W. Itin after a period of one year from the effective date of this order, or Rene F. Campeau, after a period of six (6) months from the effective date of this order, may become associated with a registered broker-dealer in a non-supervisory capacity upon an appropriate showing to the staff of the Commission that he will be adequately supervised; that George A. Reuter is expelled from the Detroit Stock Exchange; and that George A. Reuter, Charles H. Bruce, and Robert O. Safford are each suspended from association with a broker-dealer for a period of six months from the effective date of this order.

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

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

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

Warren E. Blair

Warren E. Blair
Hearing Examiner

Washington, D. C.
February 24, 1967