

sec news digest

Issue 96-65

April 9, 1996

COMMISSION ANNOUNCEMENTS

NOTICE OF SYMPOSIUM PARTICIPANTS

The Commission previously announced on February 28 that it would hold a symposium on issues related to the financial accounting and reporting of intangible assets. In connection with that announcement, the Commission is publishing a notice of the participants in the symposium (Rel. 34-36957). The symposium will be held on Thursday, April 11, 1996 from 1:00 p.m. to 5:30 p.m., and on Friday, April 12, 1996 from 9:00 a.m. to 4:30 p.m., in Room 1C30 at Commission headquarters. The symposium is open to the public.

For planning purposes, persons interested in attending the symposium are encouraged to contact Terry Warfield at (202) 942-4400 or Andre Owens at (202) 942-0800.

ENFORCEMENT PROCEEDINGS

ORDER INSTITUTING PUBLIC ADMINISTRATIVE PROCEEDINGS, MAKING FINDINGS, IMPOSING REMEDIAL SANCTIONS, AND ISSUING CEASE AND DESIST ORDER ENTERED AGAINST GRUNTAL & CO., INCORPORATED

The Commission announced that it simultaneously instituted and settled administrative and cease-and-desist proceedings against Gruntal & Co., Incorporated (Gruntal). Gruntal consented to the Order without admitting or denying the Commission's findings. The Order directs Gruntal to (1) cease and desist from committing or causing violations of Section 17(a) of the Securities Act of 1933, Sections 10(b), 15(c) and 17(a) of the Securities Exchange Act of 1934 and Rules 10b-3, 10b-5, 10b-10, 15c1-2 and 17a-3(a)(6) thereunder, and Sections 204, 206(1), 206(2), 206(3) and 207 of the

Investment Advisers Act of 1940 (Advisers Act) and Rule 204-2 thereunder; (2) pay a civil penalty of \$1 million; and (3) comply with certain undertakings.

The Order finds: Gruntal executed at least 8,813 securities transactions on behalf of investment advisory clients on a principal or agency cross basis, contrary to the disclosure in Gruntal's Forms ADV and, in many instances, in violation of the notice and consent requirements of the Advisers Act. These violations occurred after an examination by the Commission's staff identified similar violations, and after Gruntal informed the staff that it was adopting procedures to prevent future violations.

In addition, Gruntal imposed transaction charges on certain advisory clients who were already paying all-inclusive asset-based fees; issued trade confirmations wrongly identifying certain principal transactions as agency transactions; failed to disclose in its Forms ADV that it received payment for directing order flow to two affiliated broker-dealers; and failed to maintain accurate records concerning the capacity in which it executed transactions. (LR-14865; Rels. 33-7278; 34-37084; IA-1560)

ADMINISTRATIVE PROCEEDING AGAINST GRUNTAL & CO., INCORPORATED AND GRUNTAL FINANCIAL CORP. AND CIVIL INJUNCTIVE ACTION AGAINST EDWARD BAO

The Commission today instituted administrative proceedings against Gruntal & Co., Incorporated (Gruntal), a registered broker-dealer, and Gruntal Financial Corp. (Gruntal Financial). The Commission's Order found that Gruntal and Gruntal Financial violated the antifraud, reporting, and books and records provisions of the federal securities laws in connection with three separate schemes in which over \$11 million of securities and funds were diverted intentionally from customer accounts, customer and vendor checks, dividend overages, and other sources by certain members of Gruntal senior management (who are no longer associated with the firm). Approximately \$5 million of the diverted assets were transferred to Gruntal's profit and loss accounts or used to make off-books payments of Gruntal expenses. The remaining \$6 million of the diverted assets were embezzled by certain of the members of Gruntal senior management implementing the schemes.

Simultaneous with the institution of the Administrative proceeding, and without admitting or denying the findings contained therein, Gruntal and Gruntal Financial consented to the issuance of the Commission Order which, among other remedial sanctions, orders Gruntal and Gruntal Financial to disgorge \$5.5 million and Gruntal to pay a civil penalty of \$4 million.

In connection with the Order, the Commission today filed a petition in U.S. District Court for the Southern District of New York seeking a court order establishing a disgorgement process subject to the court's control. Gruntal and Gruntal Financial each consented to the entry of such an order.

The Commission also filed a complaint in U.S. District Court for the Southern District of New York today against Edward E. Bao (Bao), a former executive vice president and director of both Gruntal and Gruntal Financial. The Commission's complaint alleges violations of the antifraud and certain of the reporting provisions of the federal securities laws in connection with Bao's role in the scheme to divert assets to Gruntal's profit and loss accounts. Additionally, the complaint alleges violations of the antifraud provisions in connection with illegal trading in the securities of Gruntal Financial by Bao.

The Commission's complaint seeks a permanent injunction, an order permanently barring Bao from acting as an officer or director of any public company, and an order requiring Bao to disgorge his illegal trading profits and losses avoided, and prejudgment interest thereon. (LR-14865; Rels. 33-7279; 34-37085; AAER-771)

COMMISSION IMPOSES SANCTIONS AGAINST CALVIN WORD

The Commission has issued an Order Making Findings and Imposing Sanctions against Calvin L. Word (Word), in an administrative proceeding instituted on September 28, 1995. Word was formerly associated with First Alliance Securities, Inc. (First Alliance), a now defunct penny stock broker-dealer headquartered in Atlanta, Georgia. The Commission accepted Word's Offer of Settlement in which, without admitting or denying the Commission's findings, except for findings that he was associated with First Alliance as its vice president from February 1989 through August 1989, and that on October 27, 1994, he was convicted of conspiracy to commit securities fraud, Word consented to be barred from associating with any broker, dealer, municipal securities dealer, investment adviser or investment company, and from participating in an offering of penny stock.

The count of the indictment of which Word was convicted alleged, among other things, that Word made, and caused the First Alliance sales staff to make, material misrepresentations concerning the liquidity, suitability, and level of risk of stocks promoted by First Alliance, the current available market prices for those stocks, and the operations, financial condition and prospects of the purported issuers of those stocks. Word was sentenced to sixty months imprisonment and restitution of \$2.5 million. (Rel. 34-37082)

INVESTMENT COMPANY ACT RELEASES

QUALIVEST FUNDS, ET AL.

A notice has been issued giving interested persons until April 30 to request a hearing on an application filed by Qualivest Funds, et al. for an order under Section 6(c) of the Investment Company Act exempting applicants from Section 12(d)(1) of the Act and under Sections 6(c) and 17(b) of the Act exempting applicants from Section 17(a) of the Act. The order would permit series of the Qualivest Funds to operate as "funds of funds" by investing substantially all of their assets in other series of Qualivest Funds. (Rel. IC-21874 - April 5)

SELF-REGULATORY ORGANIZATIONS

WITHDRAWALS GRANTED

An order has been issued granting the application of PLM Equipment Growth Fund II to withdraw from listing and registration on its Limited Partnership Depository Units on the American Stock Exchange. (Rel. 34-37079)

An order has been issued granting the application of PLM Equipment Growth, Fund III to withdraw from listing and registration on its Limited Partnership Depository Units on the American Stock Exchange. (Rel. 34-37080)

An order has been issued granting the application of PLM Equipment Growth Fund to withdraw from listing and registration its Limited Partnership Depository Units on the American Stock Exchange. (Rel. 34-37081)

PROPOSED RULE CHANGE

The Pacific Stock Exchange has filed a proposed rule change (SR-PSE-96-07) to revise the Exchange's membership rules. Publication of the proposal is expected in the Federal Register during the week of April 8. (Rel. 34-37076)

APPROVAL OF PROPOSED RULE CHANGE

The Commission has approved a proposed rule change (SR-Phlx-95-86) filed by the Philadelphia Stock Exchange with respect to index options exercise advices. (Rel. 34-37077)

SIGNIFICANT NO-ACTION, EXEMPTIVE AND INTERPRETIVE LETTERS

The following is a list of significant no-action and interpretative letters recently issued by the Division of Corporation Finance. These letters express the view of the Division respecting novel or important questions arising under the Securities Act of 1933, the Securities Exchange Act of 1934, the Trust Indenture Act of 1939, the Investment Company Act of 1940, and the Investment Advisers Act of 1940. Copies of these letters may be obtained by writing to the Public Reference Room, Securities and Exchange Commission, Washington, D.C. 20549, or by making a request in person at the Public Reference Room, 450 Fifth Street, N.W., Room 1024, Washington, D.C., stating the name of the subject company, the Act and the Section of the Act to which it relates, and the public availability date.

<u>COMPANY</u>	<u>ACT/SECTION/RULE OR RELEASE</u>	<u>DATE MAILED</u>	<u>PUBLIC AVAILABILITY DATE</u>
New York Life Settlement Corporation Structured Settlement Program	1933 Act - Section 5 1940 Act - Section 8	12/22/95	12/22/95
The Morgan Health Group, Inc.	1933 Act - Rule 701(b)(1)	12/18/95	12/18/95
Rule 701(a) Interpretation	1933 Act - Rule - 701(a)	12/21/95	12/21/95

SECURITIES ACT REGISTRATIONS

The following registration statements have been filed with the SEC under the Securities Act of 1933. The reported information appears as follows: Form, Name, Address and Phone Number (if available) of the issuer of the security; Title and the number and/or face amount of the securities being offered; Name of the managing underwriter or depositor (if applicable); File number and date filed; Assigned Branch; and a designation if the statement is a New Issue.

- SB-2 GMI 96 LLC, 1217 SOUTH GRANDVIEW BLVD, WAUKESHA, WI 53188 (414) 521-2500
- 1,200 (\$3,000,000) COMMON STOCK. (FILE 333-2578-C - MAR. 20) (BR. 5
- NEW ISSUE)
- S-8 LIFERATE SYSTEMS INC, 7210 METRO BLVD, MINNEAPOLIS, MN 55439
(612) 844-0599 - 750,000 (\$6,015,000) COMMON STOCK. (FILE 333-2850 -
MAR. 29) (BR. 10)
- SB-2 AMERICAN EQUITIES INCOME FUND INC, EAST 80 ROUTE 4, PARAMUS, NJ 07652
(201) 368-5900 - 15,000,000 (\$15,000,000) STRAIGHT BONDS. (FILE 333-2856 -
MAR. 29) (BR. 12 - NEW ISSUE)
- S-8 USANA INC, 4550 SOUTH MAIN STREET, SALT LAKE CITY, UT 84107
(801) 288-2290 - 300,000 (\$2,925,000) COMMON STOCK. (FILE 333-2860 -
MAR. 29) (BR. 4)
- S-8 INTERNATIONAL STANDARDS GROUP LIMITED, 3200 N MILITARY TRAIL STE 210,
BOCA RATON, FL 33431 (407) 997-5880 - 600,000 (\$525,000) COMMON STOCK.
(FILE 333-2864 - MAR. 29) (BR. 9)
- S-8 UNITED VIDEO SATELLITE GROUP INC, 7140 S LEWIS AVENUE, TULSA, OK 74136
(918) 488-4000 - 200,000 (\$4,487,500) COMMON STOCK. (FILE 333-2866 -
MAR. 29) (BR. 7)
- S-8 MOBILE MINI INC, 1834 W 3RD ST, TEMPE, AZ 85281 (602) 894-6311 - 75,000
(\$283,500) COMMON STOCK. (FILE 333-2868 - MAR. 29) (BR. 9)
- S-1 FINE HOST CORP, 3 GREENWICH OFFICE PARK, GREENWICH, CT 06831
(203) 629-4320 - 4,312,500 (\$64,687,500) COMMON STOCK. (FILE 333-2906 -
MAR. 29) (BR. 12 - NEW ISSUE)
- S-4 AMERICA FIRST APARTMENT INVESTORS LP, 1004 FARNUM ST, STE 400, OMAHA, NE
68102 (402) 444-1630 - 5,245,623 (\$47,210,607)
COMMON SHARES OF BENEFICIAL INTEREST. (FILE 333-2920 - MAR. 29) (BR. 11
- NEW ISSUE)
- F-6 AO TRADE HOUSE GUM, 48 WALL ST, C/O BANK OF NEW YORK, NEW YORK, NY 10286
(212) 495-1727 - 20,000,000 (\$1,000,000)
DEPOSITARY RECEIPTS FOR COMMON STOCK. (FILE 333-2922 - MAR. 29) (BR. 99
- NEW ISSUE)
- S-1 TREX MEDICAL CORP, 36 APPLE RIDGE RD, DANBURY, CT 06810 - \$20,000,000
COMMON STOCK. (FILE 333-2924 - MAR. 29) (BR. 7)
- S-1 TREX MEDICAL CORP, 36 APPLE RIDGE RD, DANBURY, CT 06810 - \$38,640,000
COMMON STOCK. (FILE 333-2926 - MAR. 29) (BR. 7 - NEW ISSUE)
- S-8 USANA INC, 4550 SOUTH MAIN STREET, SALT LAKE CITY, UT 84107
(801) 288-2290 - 700,000 (\$6,790,000) COMMON STOCK. (FILE 333-2934 -
MAR. 29) (BR. 4)



U.S. Securities and Exchange Commission
Washington, D.C. 20549 (202) 942-0020

News
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FOR IMMEDIATE RELEASE

96-59

SEC TO CONSIDER ONE ITEM AT AN OPEN MEETING

Washington, D.C., April 9, 1996 -- The Securities and Exchange Commission will consider one item at an open meeting to be conducted under the Government in the Sunshine Act on Wednesday, April 10, at 10:00 a.m. The meeting will be held in Room 1C30, at Commission Headquarters, 450 Fifth Street, N.W., Washington, D.C. The item for discussion is:

- whether to propose a new regulation containing anti-manipulation rules governing securities offerings. The new regulation would simplify, modify, and, in some cases, eliminate provisions that otherwise restrict the activities of issuers, underwriters, and others participating in a securities offering. The new regulation is proposed to be adopted under various provisions of the Securities Act of 1933 and Securities Exchange Act of 1934 (Exchange Act) and, if adopted, would replace current Rules 10b-6, 10b-6A, 10b-7, 10b-8 and 10b-21 under the Exchange Act. Related amendments to Items 502(d) and 508 of both Regulation S-B And S-K, and to Rules 10b-18 and 17a-2 under the Exchange Act, also will be considered.

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Any member of the public who requires auxiliary aids such as a sign-language interpreter or material on tape to attend a public meeting should contact Nancy Wolynetz, Office of Administrative and Personnel Management, to make arrangements. Ms. Wolynetz can be reached at (202) 942-4091, or at a TTY number (202) 942-4075. Staff members at the Commission are encouraged to contact Ms. Wolynetz if they receive inquiries on availability of auxiliary aids.



U.S. Securities and Exchange Commission
Washington, D.C. 20549 (202) 942-0020

**News
Release**

FOR IMMEDIATE RELEASE

96-60

IN THE MATTER OF CALVIN L. WORD

Washington, D.C., April 9, 1996 -- The Securities and Exchange Commission announced today that it has issued an Order Making Findings and Imposing Sanctions Pursuant to Sections 15(b) and 19(h) of the Securities Exchange Act of 1934, against Calvin L. Word (Word), in an administrative proceeding instituted on September 28, 1995. Word was formerly associated with First Alliance Securities, Inc. (First Alliance), a now defunct penny stock broker-dealer headquartered in Atlanta, Georgia.

Word submitted an Offer Of Settlement, which the Commission has determined to accept, in which he consented to the Order without admitting or denying the Commission's findings, except for findings that he was associated with First Alliance as its vice president from February 1989 through August 1989, and that on October 27, 1994, in the United States District Court for the Northern District of Georgia, he was convicted of conspiracy to commit securities fraud based upon his conduct while at First Alliance. See U.S. v. William F. Lincoln, et al., Criminal Action No. 1:93-CR-506-GET-4 (N.D. Ga.). On March 8, 1995, Word was sentenced to sixty months imprisonment, three years supervised release and restitution of \$2.5 million.

The count of the indictment of which Word was convicted alleged, among other things, that Word made, and caused the First Alliance sales staff to make, material misrepresentations concerning the liquidity, suitability, and level of risk of stocks promoted by First Alliance, the current available market prices for those stocks, and the operations, financial condition and prospects of the purported issuers of those stocks.

The Commission's Order barred Word from association with any broker, dealer, municipal securities dealer, investment adviser or investment company. The Order further barred him from participating in an offering of penny stock.

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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C.

LITIGATION RELEASE NO. 14865 / April 9, 1996

In the Matter of GRUNTAL & CO., INCORPORATED and GRUNTAL
FINANCIAL CORP., Administrative Proceeding File No. 3-8984

SECURITIES AND EXCHANGE COMMISSION v. GRUNTAL & CO., INCORPORATED
and GRUNTAL FINANCIAL CORP., 96 Civ. 2514 (MBM) (S.D.N.Y. 1996)

SECURITIES AND EXCHANGE COMMISSION v. EDWARD E. BAO, 96 Civ. 2515
(MBM) (S.D.N.Y. 1996)

In the Matter of GRUNTAL & CO., INCORPORATED, Administrative
Proceeding File No. 3-8983

The Securities and Exchange Commission ("Commission") today instituted and simultaneously settled administrative proceedings against Gruntal & Co., Incorporated ("Gruntal"), a registered broker-dealer, and Gruntal Financial Corp. ("Gruntal Financial"), which operates a brokerage business through Gruntal, its wholly owned subsidiary, and was a public reporting company from 1983 to 1987. In addition, the Commission today filed a complaint in U.S. District Court for the Southern District of New York against Edward E. Bao ("Bao"), a former executive vice president and director of both Gruntal and Gruntal Financial.

GRUNTAL AND GRUNTAL FINANCIAL SETTLE CHARGES OF SECURITIES LAW
VIOLATIONS IN CONNECTION WITH DIVERSIONS OF CUSTOMER AND OTHER
THIRD PARTY ASSETS

In the first of two separate administrative Orders issued today, the Commission found that Gruntal and Gruntal Financial violated the antifraud, reporting, and books and records provisions of the federal securities laws in connection with three separate schemes to divert assets that occurred between 1984 and 1994 and that were instituted by certain members of Gruntal senior management (who are no longer associated with the firm). Simultaneous with the institution of the administrative proceeding, and without admitting or denying the findings contained therein, Gruntal and Gruntal Financial consented to the issuance of the Commission Order which, among other remedial sanctions, orders Gruntal and Gruntal Financial to disgorge \$5.5 million and Gruntal to pay a civil penalty of \$4 million.

The Findings

The Commission Order finds that, among other things, beginning in 1984 and continuing for a decade, certain members of Gruntal senior management intentionally diverted securities and funds totaling over \$11 million from customer accounts, customer and vendor checks, dividend overages, and other sources at Gruntal. Also beginning in 1984, certain senior managers at Gruntal opened securities accounts at Gruntal under fictitious customer names. Approximately \$5 million of the diverted assets were moved to the fictitious customer accounts and then transferred to Gruntal's profit and loss accounts or used to make off-books payments of Gruntal expenses. The remaining \$6 million of the diverted assets were embezzled by certain of the members of Gruntal senior management implementing the schemes.

The Order also finds that, in furtherance of these schemes, the senior Gruntal managers implementing the diversions falsified Gruntal's books and records. Other books and records, although not intentionally falsified, were based upon information contained in the falsified records and therefore were inaccurate. As a result of the diversions, Gruntal filed periodic FOCUS reports that overstated firm income, and Gruntal Financial filed false and misleading periodic reports and a false and misleading registration statement that mischaracterized the diverted assets and misstated Gruntal Financial's income. Gruntal Financial's filings also failed to disclose the involvement of certain senior officers and managers in the diversions of customer and other third party assets to income.

The Order finds that Gruntal Financial violated Section 17(a) of the Securities Act of 1933 ("Securities Act") and Sections 10(b), 13(a), 13(b)(2)(A), and 13(b)(5) of the Securities Exchange Act of 1934 ("Exchange Act") and Rules 10b-5, 12b-20, 13a-1, 13a-13, and 13b2-1 thereunder. The Order further finds that Gruntal willfully violated Section 17(a) of the Securities Act and Sections 10(b), 15(c)(1), 17(a), and 17(e) of the Exchange Act and Rules 10b-5, 17a-3, 17a-4, 17a-5(a), 17a-5(d), and 17a-11(d) thereunder, and willfully aided, abetted, and caused Gruntal Financial's violations of Section 17(a) of the Securities Act and Sections 10(b), 13(a), 13(b)(2)(A), and 13(b)(5) of the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-13, and 13b2-1 thereunder.

The Remedial Sanctions

In addition to other remedial sanctions, the Order:

- censures Gruntal;
- orders Gruntal and Gruntal Financial to cease and desist from committing or causing any violation, and any future violation, of the antifraud and other provisions of the federal securities laws;

- requires Gruntal to pay a civil penalty of \$4 million;
- requires Gruntal and Gruntal Financial to pay \$5.5 million in disgorgement and prejudgment interest;
- requires Gruntal and Gruntal Financial to hire an independent person to verify Gruntal's representation that it has already repaid, recredited, escheated, or properly segregated and scheduled for escheatment an additional \$6.7 million in connection with the conduct described in the Commission's Order; and
- requires Gruntal and Gruntal Financial to hire an independent consultant to (1) conduct a thorough review of Gruntal's policies and procedures concerning, among other things, its back office operations and compliance, and (2) investigate Gruntal's order execution and reporting practices for Over-The-Counter ("OTC") securities transactions. It also requires Gruntal and Gruntal Financial, from their own funds, to directly reimburse any customer identified by the independent consultant as having been harmed by Gruntal's OTC trading practices.

In connection with the Commission's Order, the Commission today filed a petition in U.S. District Court for the Southern District of New York seeking a court order establishing a disgorgement and distribution process administered by an independent person subject to the control of the Court. Gruntal and Gruntal Financial each consented to the entry of such an order.

The Commission's investigation in this matter is continuing as to other entities and individuals.

The Commission acknowledges the assistance of the New York Stock Exchange, Inc. in this matter.

COMPLAINT FILED AGAINST BAO

The complaint filed in District Court against Bao alleges violations of Section 17(a) of the Securities Act and Sections 10(b) and 13(b)(5) of the Exchange Act and Rules 10b-5, 13b2-1 and 13b2-2 thereunder in connection with the scheme to divert assets to Gruntal's profit and loss accounts. The Commission's complaint alleges that Bao conceived of and directed the scheme to divert assets from customer accounts, customer and vendor checks, unclaimed dividends, and other sources at Gruntal to the fictitious accounts, and from there to Gruntal's profit and loss accounts.

In addition, the Commission's complaint alleges that Bao violated Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder by engaging in illegal trading in connection with the sale of Gruntal Financial securities. In 1987, after the scheme had been in operation for approximately three years, Bao sold 582,000 shares of Gruntal Financial common stock for his own account and also sold another 36,000 shares he controlled as trustee. According to the complaint, in connection with those sales, Bao made certain affirmative material misrepresentations and he sold the Gruntal Financial stock while in possession of material non-public information concerning the diversion scheme, his and other senior Gruntal managers involvement in it, and Gruntal Financial's overstatements of income.

The Commission's complaint seeks a permanent injunction, an order permanently barring Bao from acting as an officer or director of any public company, and an order requiring Bao to disgorge his illegal trading profits and losses avoided, and prejudgment interest thereon.

GRUNTAL SETTLES CHARGES OF SECURITIES LAW VIOLATIONS IN ITS INVESTMENT ADVISORY BUSINESS

In a separate matter, the Commission also announced that it instituted and simultaneously settled public administrative and cease-and-desist proceedings against Gruntal involving securities law violations arising principally from Gruntal's investment advisory business. Without admitting or denying the Commission's findings, Gruntal agreed to pay a \$1 million civil penalty and consented to issuance of an Order directing that Gruntal cease and desist from future violations, pay disgorgement in amounts to be determined, and adopt various remedial procedures.

The Order makes findings concerning five areas of violative conduct:

- Between January 1993 and November 1995, Gruntal executed at least 8,813 transactions for advisory clients on a principal basis or by crossing advisory client orders with orders for other Gruntal customers. These transactions were contrary to the disclosure in Gruntal's filings with the Commission, and in many instances violated the notice and consent requirements of the Investment Advisers Act of 1940 ("Advisers Act").
- Gruntal charged commissions, commission equivalents, mark-ups and mark-downs on transactions for certain advisory clients who had chosen to pay an all-inclusive, asset-based fee, contrary to statements in

Gruntal's filings with the Commission and brochures provided to clients.

- Gruntal sent trade confirmations to advisory clients and other brokerage customers wrongly identifying certain principal transactions as agency transactions.
- From March 1995 through November 1995, Gruntal failed to disclose to its advisory clients that it received payment for directing order flow to two affiliated broker-dealers.
- Gruntal failed to maintain accurate records concerning the capacity in which it executed transactions.

The Order also makes the following findings: During an examination conducted in late 1992, the Commission's staff detected improper principal and agency cross transactions, and so informed Gruntal in a deficiency letter in January 1993. In its response letter to the staff, Gruntal represented that it was adopting review procedures and a special order ticket for advisory client trades to ensure that these practices ceased. Thereafter, Gruntal failed to institute adequate procedures, never used the new order ticket, and executed at least 8,813 violative transactions.

The Order finds that Gruntal violated Section 17(a) of the Securities Act; Sections 10(b), 15(c) and 17(a) of the Exchange Act and Rules 10b-3, 10b-5, 10b-10, 15c1-2 and 17a-3(a)(6) thereunder; and Sections 204, 206(1), 206(2), 206(3) and 207 of the Advisers Act and Rule 204-2 thereunder.

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 7279 / April 9, 1996

SECURITIES EXCHANGE ACT OF 1934
Release No. 37085 / April 9, 1996

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 771 / April 9, 1996

ADMINISTRATIVE PROCEEDING
File No. 3-8984

In the Matter of	:	
	:	
GRUNTAL & CO., INCORPORATED	:	ORDER INSTITUTING
	:	PUBLIC ADMINISTRATIVE
and	:	PROCEEDINGS, MAKING
	:	FINDINGS, IMPOSING
GRUNTAL FINANCIAL CORP.,	:	REMEDIAL SANCTIONS, AND
	:	ISSUING CEASE AND
Respondents.	:	DESIST ORDER
	:	

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be instituted against Gruntal & Co., Incorporated ("Gruntal") pursuant to Section 8A of the Securities Act of 1933 ("Securities Act") and Sections 15(b)(4) and 21C of the Securities Exchange Act of 1934 ("Exchange Act") and against Gruntal Financial Corp. ("Gruntal Financial") pursuant to Section 8A of the Securities Act and Section 21C of the Exchange Act. In anticipation of the institution of these administrative proceedings, Gruntal and Gruntal Financial have submitted Offers of Settlement, which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceeding brought by or on behalf of the Commission, or to which the Commission is a party, Gruntal and Gruntal Financial, by their Offers of Settlement, prior to a hearing pursuant to the Commission's Rules of Practice and without admitting or denying the findings set forth herein, consent to the entry of this Order Instituting Public Administrative Proceedings, Making Findings,

Imposing Remedial Sanctions, and Issuing Cease and Desist Order ("Order").

II.

Accordingly, IT IS HEREBY ORDERED that proceedings pursuant to Section 8A of the Securities Act and Sections 15(b)(4) and 21C of the Exchange Act be, and hereby are, instituted.

III.

The Commission makes the following findings:^{1/}

A. RESPONDENTS

1. Gruntal

At all times from December 15, 1983 to the present, Gruntal has been a broker-dealer registered with the Commission pursuant to Section 15(b) of the Exchange Act. Throughout that period, Gruntal has been a member of several national securities exchanges, including The New York Stock Exchange, Inc. ("NYSE"), and of the National Association of Securities Dealers, Inc. ("NASD"). As a broker-dealer, Gruntal provides a full range of securities brokerage and trading services, as well as related financial services.

From 1983 to June 1990, Gruntal conducted its back office operations through a wholly owned subsidiary, Regional Clearing Corp. ("Regional Clearing"). In June-1990, Regional Clearing was merged into Gruntal. As used in this Order, the term "Gruntal" refers, as the context requires, to Gruntal and/or Regional Clearing.

2. Gruntal Financial

From December 15, 1983 to the present, Gruntal Financial has been a Delaware corporation operating a securities brokerage business through Gruntal, its wholly owned subsidiary. For the period December 1983 to August 1987, Gruntal Financial was a publicly traded corporation with its securities registered pursuant to Section 12(b) of the Exchange Act and listed on the NYSE. From December 1983 to August 1987, Gruntal Financial was required to file periodic reports with the Commission pursuant to Section 13 of the Exchange Act. In June 1986, Gruntal Financial

^{1/} The findings herein and the entry of this Order are solely for the purposes of this proceeding and shall not be binding on any other person or entity named in any other proceeding.

conducted an offering of 7 1/2% Convertible Subordinated Debentures due 2011.

In August 1987, Gruntal Financial was acquired by The Home Group, Inc., a public corporation whose securities were registered pursuant to Section 12(b) of the Exchange Act. Gruntal Financial was held as a subsidiary of The Home Insurance Company, a wholly owned subsidiary of The Home Group, Inc. In May 1989, The Home Group, Inc. changed its name to AmBase Corporation. In February 1991, The Home Insurance Company was acquired by Home Holdings Inc., a public corporation with its securities registered pursuant to Section 12(b) of the Exchange Act. Home Holdings Inc. went private in mid-1995.

B. OTHER RELEVANT PERSON

Edward E. Bao

Edward E. Bao was Gruntal's Executive Vice President for Operations and Administration. Bao also held the same position at Gruntal Financial. Bao's employment at Gruntal and Gruntal Financial was terminated on December 16, 1994.

C. SUMMARY

This proceeding involves conduct in two areas. The first, and principal, area involves violations of the antifraud, reporting, and record-keeping provisions of the federal securities laws in connection with three separate schemes to divert assets that occurred between 1984 and 1994 and that were instituted by certain members of Gruntal senior management (who left the firm subsequent to the conduct discussed herein). In those schemes, securities and funds totalling over \$11 million were diverted intentionally from customer accounts, dividend "overages,"^{2/} customer and vendor checks, and other sources at Gruntal. Approximately \$5 million of the diverted assets were moved to fictitious customer accounts and then transferred to

^{2/} Dividend "overages" resulted at Gruntal when the firm received stock dividends, cash dividends, or interest accrued on debt securities from issuing corporations in excess of those that its books showed were due to customer or proprietary accounts. See Edward C. Jaegerman, 46 SEC 706, 708 (1976). For example, Gruntal received such dividends when its customers sold securities between their record dates and their payment dates. Those dividends did not belong to Gruntal; instead, Gruntal held them as a "debtor," with a "duty" to transmit the unclaimed dividends to their beneficial owners. See Delaware v. New York, 113 S. Ct. 1550, 1559 (1993).

Gruntal profit and loss ("P&L") accounts or used to make off-books payments of Gruntal expenses. Thus, Gruntal used these diverted assets artificially to inflate its income or reduce its expenses. The remaining \$6 million of the diverted assets were embezzled by certain members of Gruntal management implementing the schemes.

In furtherance of these schemes, the Gruntal officers and managers implementing the diversions falsified Gruntal's books and records. To carry out and conceal the diversions, they created fictitious customer accounts. Other books and records, although not intentionally falsified, were based upon information contained in the falsified records and therefore were inaccurate. The diversions were instituted originally to inflate Gruntal's income. As a result of the diversions, Gruntal filed periodic FOCUS reports that overstated firm income, and Gruntal Financial filed periodic reports that mischaracterized the diverted assets and misstated Gruntal Financial's income. These reports also failed to disclose the diversion of customer and other third party funds to income and the involvement of certain officers and managers in those activities.

The second area involves Gruntal's execution and reporting of certain Over-the-Counter ("OTC") trades. In mid-1995, NASD reports indicated that Gruntal's late reported OTC trades exceeded the industry average. Gruntal subsequently reviewed a sample of such trades and found that, in a limited number of instances, customers were financially disadvantaged in connection with these practices.

D. THE MISAPPROPRIATION SCHEMES

1. Gruntal Misappropriates Assets to Increase Its Income

a. Sources of Diverted Assets

Beginning in 1984, Bao and certain senior managers under his control identified various assets that could be diverted and, ultimately, misappropriated for Gruntal's benefit. At Bao's direction, this process was conducted initially by three members of Gruntal's senior management: its Director of Operations, its Manager of Internal Audit, and the Executive Cashier (hereinafter "Certain Senior Managers").^{3/} By 1984, these managers realized

^{3/} The misappropriation schemes came to light after the Executive Cashier's sudden, unexpected death on October 16, 1994. In November 1994, Gruntal terminated the employment of the Director of Operations and the Manager of Internal Audit. Both of those individuals subsequently have pleaded guilty to a two-count (continued...)

that hundreds of thousands of dollars worth of overages had accrued in Gruntal dividend payable accounts.^{4/} At the behest of Bao -- the number two officer at Gruntal -- Certain Senior Managers undertook to ascertain to whom the overages belonged and the likelihood that Gruntal might yet receive claims for them. Overages that were unlikely to be claimed became candidates for diversion.

The overages were potentially escheatable property. Thus, if they had remained unclaimed, Gruntal should have eventually escheated them to the states. Instead, Bao and Certain Senior Managers diverted unclaimed overages out of the dividend accounts.

In about 1987 or 1988, Bao and Certain Senior Managers realized that Gruntal's bank reconciliation accounts held stale or outstanding customer and vendor checks that Gruntal could misappropriate. Gruntal's normal procedures required it to notify its customers of the checks. If the checks remained unclaimed after such notification, Gruntal was required eventually to pay them to the appropriate states. Gruntal did abide by these procedures for checks of smaller denominations; however, larger checks were diverted out of the bank reconciliation accounts.^{5/}

In addition, Gruntal, acting through Bao and Certain Senior Managers, diverted assets from dormant customer accounts. Securities and customer money balances were transferred out of customer accounts that were inactive or for which mailed account statements had been returned.

b. Fictitious Accounts and Falsified Records Hide the Diverted Assets

Beginning in 1984, Bao and Certain Senior Managers opened securities accounts at Gruntal under fictitious customer names.

^{3/}(...continued)

criminal information filed by the United States Attorney's Office for the Southern District of New York.

^{4/} Gruntal used these accounts to receive, hold, and disburse the stock dividends, cash dividends, and accrued interest that it received from issuing corporations.

^{5/} Notification of customers who had "stale" checks was more than a mere pro forma procedure. In many cases, these checks did belong to present, living customers. In fact, during the course of the diversions, Certain Senior Managers were forced to re-credit to customers over \$700,000 for previously diverted checks when customers contacted Gruntal inquiring about their money.

These accounts were given numbers purporting to identify them as customer accounts. From 1984 and continuing for a decade, dividend overages, stale checks, and other assets targeted for diversion were transferred into these fictitious customer accounts. To avoid detection and to obscure the true nature of the assets, these transfers often were made by means of complex, multiple-step transactions that utilized otherwise legitimate Gruntal operational or suspense accounts as interim stopping points. From fictitious customer accounts, diverted assets were transferred into the firm's P&L accounts and falsely credited as income.^{6/} These transfers tended to coincide with downturns in Gruntal's monthly income. Sometimes the diverted assets were used to make off-books payments of firm expenses, thereby reducing Gruntal's liabilities.

In carrying out the scheme, Gruntal, acting through Bao and Certain Senior Managers, created, or caused to be created, numerous fictitious and false books and records, including account opening documents, account statement entries, debit and credit memos, dividend claim forms, and accounting and journal entries.^{7/} In addition, to avoid detection, Bao and Certain Senior Managers periodically closed the fictitious customer accounts and opened new accounts to take their place, utilizing a number of fictitious accounts over time. Finally, Gruntal, through Bao and Certain Senior Managers, circumvented and disregarded certain procedures and internal controls, in particular those relating to opening new accounts and the proper handling of abandoned and/or escheatable property.

2. Embezzlement of Diverted Assets

a. Certain Senior Managers Divert Assets for Their Own Benefit

In about 1987, Certain Senior Managers began to divert assets for their own benefit. Their scheme drew on the same sources of assets utilized in the original diversions and largely used the same methods for diverting those assets. For their scheme also, Certain Senior Managers created, or caused to be created, fictitious or false records. However, this second

^{6/} In some instances, the diversions bypassed the fictitious customer accounts, and items were moved from their sources to operational or suspense accounts and from those accounts directly to Gruntal's P&L.

^{7/} The implementation and concealment of the scheme was effectively assisted -- knowingly, recklessly, or inadvertently -- by individuals from several departments at Gruntal, including bank reconciliation, abandoned property, internal audit, accounting, and the back office.

scheme largely avoided the fictitious customer accounts, and the assets diverted under this scheme ultimately left the firm -- without the authorization of other officers at Gruntal.

b. Executive Cashier Diverts Assets for His Own Use

A third diversion scheme developed when the Executive Cashier began an embezzlement on his own behalf. The Executive Cashier implemented a scheme based primarily on the creation of debits in Gruntal's reorganization account and which ultimately involved the creation, in some instances, of false "fails to deliver."^{8/} He then directed the alteration and falsification of Gruntal's corresponding records. Only a small portion of the assets the Executive Cashier embezzled came from the sources of assets used in the other diversion schemes. The Executive Cashier's scheme was conducted without the authorization of other officers at Gruntal.

E. FALSE FILINGS

1. Gruntal Financial

From 1985 through mid-1987, Gruntal Financial filed with the Commission false and misleading periodic reports and a false and misleading registration statement. Those reports, including the financial statements contained therein, were misstated because they failed to reflect, disclose, or correctly characterize the amounts and uses of the diverted assets. As a result, Gruntal Financial's income was overstated. Because a large number of Gruntal Financial's books and records were falsified, it is not always possible to quantify the precise impact of the diversions on income during this period. Nevertheless, for some periods, the misstatement of income can be clearly ascertained. For example, as a result of the diversions, Gruntal Financial's annual report on Form 10-K for fiscal year 1985 overstated its pre-tax income by approximately 15%. In addition, Gruntal Financial's periodic reports and registration statement failed to disclose the diversion of customer and other third party funds to income and management's role in those activities.

The false and misleading Gruntal Financial filings include:

^{8/} A fail to deliver occurs when the selling broker-dealer, in this case Gruntal, has failed to deliver securities to the buying broker-dealer. The selling broker-dealer will not receive payment as long as the fail continues. Thus, the creation of a false fail to deliver created the appearance that monies actually missing were merely monies that were owed to, and had not yet been received by, Gruntal.

(1) A registration statement on Form S-1, filed on June 2, 1986, and Amendment No. 1 thereto, filed on June 18, 1986, both filed in connection with Gruntal Financial's offering of 7 1/2% Convertible Subordinated Debentures due June 15, 2011;

(2) Annual reports on Form 10-K for the years 1985 and 1986; and

(3) A quarterly report on Form 10-Q for the third quarter of fiscal year 1987.

2. Gruntal

Between 1985 and 1994, Gruntal filed false and misleading FOCUS reports with the Commission and with the NYSE. These reports, including the income statements contained therein, overstated Gruntal's income. Because Bao and Certain Senior Managers falsified a large number of Gruntal's books and records, it is not always possible to quantify the precise impact of the diversions on the firm's income during this period. Nevertheless, for some periods, the misstatement can be clearly ascertained. For example, by diverting assets to income, Gruntal falsely overstated its pre-tax income by approximately 13% on its 1985 annual FOCUS report. Similarly, Gruntal's quarterly FOCUS report on Form X-17A-5 for the quarter ended June 28, 1991, overstated pre-tax income by approximately 130%.

The false Gruntal filings include:

(1) Annual FOCUS reports for fiscal years 1985 through 1994;

(2) Certain quarterly FOCUS reports on Form X-17A-5 from second quarter 1986 through fourth quarter 1994; and

(3) Certain monthly FOCUS reports on Form X-17A-5 for months from April 1986 through October 1994.

F. LATE REPORTING AND ORDER EXECUTION PRACTICES

In mid-1995, NASD reports issued to Gruntal indicated that Gruntal's late reported OTC trades exceeded the industry average. In November 1995, Gruntal undertook a study aimed at finding the reasons for the late reported trades. As part of that study, Gruntal examined a random sample of those trades. Gruntal found that, in a limited number of instances, customers had been financially disadvantaged by Gruntal's trading practices. For example, Gruntal identified two instances in which a customer placed an order to buy a particular OTC stock, but the order was not executed in a timely manner. Gruntal's trading desk, which had started the day flat with regard to that particular stock, subsequently built a position in it. Once that position was

built, the customer's order was filled from the position, to the customer's detriment. Gruntal has repaid those disadvantaged customers that it has identified to date.

A broker-dealer which fails to transmit promptly information required by an effective transaction reporting plan with respect to a reported security violates Section 11A(a)(2) of the Exchange Act and Rule 11Aa3-1(c) thereunder. A broker-dealer which fails to execute a customer's order promptly in accordance with the customer's instructions without disclosure violates the antifraud provisions, including Sections 10(b) and 15(c) of the Exchange Act and Rules 10b-5 and 15c2-1 thereunder and Section 17(a) of the Securities Act. As set forth below in Section VI.F.2. of this Order, an Independent Consultant acceptable to the Commission's staff will investigate the OTC order execution and reporting practices set forth above and, among other things, will direct Gruntal to reimburse any customers who have been financially harmed in connection with Gruntal's processing of OTC trades.

IV.

A. VIOLATIONS OF THE ANTIFRAUD PROVISIONS

Section 17(a) of the Securities Act proscribes fraud in connection with the "offer or sale" of securities. Section 10(b) of the Exchange Act and Rule 10b-5 thereunder prohibit fraud in connection with the purchase or sale of a security. Section 15(c)(1) of the Exchange Act prohibits a broker-dealer from effecting transactions in securities, otherwise than on a national securities exchange of which it is a member, by means of any manipulative, deceptive, or fraudulent device or contrivance.

A broker-dealer is entrusted with the funds and securities of its customers. Customers rely upon their brokerage. But, from 1984 through 1994, Bao and Certain Senior Managers took assets in the form of customer securities and balances, stale customer and vendor checks, and unclaimed dividends. They took pains to hide their actions.

A broker-dealer's misappropriation of customer securities is a violation of the antifraud provisions of the federal securities laws. Donald T. Sheldon, 51 SEC 59, 62-63 & n.11 (1992), aff'd, 45 F.3d 1515 (11th Cir. 1995). "[I]t is a fraudulent and deceptive act, practice, and course of business, which operates as a fraud and deceit on a customer, for a broker-dealer to . . . convert to his own use customers' funds or fully-paid for securities of customers held by the broker-dealer for safe-keeping." Sheldon, 51 SEC at 62 n.10 (quoting Ezra Weiss, Registration and Regulation of Brokers and Dealers 181 (1965)). At Gruntal, a substantial amount of customer funds and securities

were converted for the broker-dealer's use. Gruntal also violated the antifraud provisions when it misappropriated unclaimed dividend overages held in its dividend accounts and converted the dividends for firm use. Edward C. Jaegerman, 46 SEC 706, 708-09 (1976).

The "in connection with" requirement of the antifraud provisions "is met if the fraud alleged 'somehow touches upon' or has 'some nexus' with 'any securities transaction.'" SEC v. Rana Research, Inc., 8 F.3d 1358, 1362 (9th Cir. 1993) (quoting SEC v. Clark, 915 F.2d 439, 449 (9th Cir. 1990)).^{9/} Transactions in securities were integral to the fraudulent activities at Gruntal. Gruntal officers and managers removed balances and securities from customers' securities accounts, purchased securities with the stolen balances, sold customers' securities, took customer checks representing proceeds of securities transactions, and misappropriated dividends payable to contra-brokers, institutional investors, and Gruntal's customers.

To violate Section 17(a)(1), Section 10(b), or Rule 10b-5, a defendant must act with scienter. Aaron v. SEC, 446 U.S. 680, 701-02 (1980). Bao and Certain Senior Managers at Gruntal and Gruntal Financial knowingly instituted and condoned the diversions. Gruntal and Gruntal Financial are chargeable with their employees' state of mind. See SEC v. Manor Nursing Ctrs., Inc., 458 F.2d 1082, 1089 n.3 (2d Cir. 1972).

From 1985 through mid-1987, Gruntal Financial itself violated the antifraud provisions by filing certain materially false and misleading reports. Gruntal Financial was a holding company conducting its business through Gruntal. The original diversion scheme was instituted by Gruntal to inflate its income. As a result of Gruntal's overstated income, Gruntal Financial's income was also inflated, and Gruntal Financial filed with the Commission periodic reports and a registration statement that were materially misstated -- mischaracterizing the diverted assets and overstating income.^{10/} Gruntal Financial's filings were also made materially misleading by their failure to disclose

^{9/} Although the courts are in some disagreement over the contours of the "in connection with" requirement for a private plaintiff, "its meaning in SEC actions remains as broad and flexible as is necessary to accomplish the statute's purpose of protecting investors." Rana Research, 8 F.3d at 1362 (discussing requirement in context of case brought under Section 10(b)).

^{10/} A fact is material if there is a substantial likelihood that a reasonable investor would consider the information to be important. Basic Inc. v. Levinson, 485 U.S. 224, 231-32 (1988). Information regarding a company's income is among the most important information for making an investment decision.

the diversions at Gruntal or the involvement of certain members of senior management. See SEC v. Kalvex Inc., 425 F. Supp. 310, 315-16 (S.D.N.Y. 1975); cf. SEC v. Scott, 565 F. Supp. 1513, 1527 (S.D.N.Y. 1983) (stating that failure to disclose kickback scheme involving principal obviously material), aff'd sub nom. SEC v. Cayman Islands Reinsurance Corp., 734 F.2d 118 (2d Cir. 1984). During this period, Gruntal Financial securities were listed and traded on the NYSE, and, in June 1986, Gruntal Financial conducted an offering of Convertible Subordinated Debentures.

In order to establish liability for aiding and abetting, the Commission must establish (1) the existence of a primary violation, (2) that the aider or abettor had a general awareness that his role was part of an overall activity that was improper, and (3) that the aider or abettor knowingly and substantially assisted the principal violation. Dominick & Dominick, Inc., 50 SEC 571, 577 (1991).

Gruntal willfully aided, abetted, and caused Gruntal Financial's violations of the antifraud provisions. Gruntal, acting through Bao and Certain Senior Managers, knowingly implemented and condoned a scheme by which assets were transferred fraudulently and Gruntal's income was artificially inflated. As a result of that scheme, Gruntal Financial filed with the Commission materially misstated reports.

For the foregoing reasons, Gruntal willfully violated Section 17(a) of the Securities Act, Sections 10(b) and 15(c)(1) of the Exchange Act, and Rule 10b-5 thereunder by fraudulent transactions and practices, and Gruntal Financial violated Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder by material misrepresentations and omissions in its periodic reports and registration statement. Moreover, Gruntal willfully aided, abetted, and caused Gruntal Financial's violations.

B. GRUNTAL FINANCIAL'S VIOLATIONS OF EXCHANGE ACT REPORTING AND RECORD-KEEPING PROVISIONS

Section 13(a) of the Exchange Act and Rules 13a-1 and 13a-13 thereunder require issuers with securities registered under Section 12 of the Exchange Act to file annual and quarterly reports with the Commission and to keep this information current. The obligation to file such reports embodies the requirement that they be true and correct. See, e.g., SEC v. Savoy Indus., Inc., 587 F.2d 1149, 1165 (D.C. Cir. 1978), cert. denied, 440 U.S. 913 (1979). Exchange Act Rule 12b-20 further requires the inclusion of any additional material information that is necessary to make required statements, in light of the circumstances under which they were made, not misleading. Information regarding the

financial condition of a company is presumptively material. SEC v. Blavin, 760 F.2d 706, 711 (6th Cir. 1985).

As discussed above, from 1985 through mid-1987 Gruntal Financial filed certain false and misleading periodic reports with the Commission that mischaracterized the diverted assets, misstated Gruntal Financial's income, and failed to disclose management's role in the diversion of customer and other third party funds to income.

Section 13(b) (2) (A) of the Exchange Act requires Section 12 registrants to make and keep books, records, and accounts accurately reflecting transactions involving their assets. Section 13(b) (5) of the Exchange Act provides that no person shall knowingly falsify any such book, record, or account or circumvent internal controls. Rule 13b2-1 also prohibits the falsification of any book, record, or account subject to Section 13(b) (2) (A).

From 1984 through mid-1987, Gruntal Financial's books and records reflecting transactions in its assets were not merely inaccurate, they were intentionally falsified. Its internal accounting controls were intentionally circumvented.

For the foregoing reasons, Gruntal Financial violated Section 13(a), 13(b) (2) (A), and 13(b) (5) and Rules 12b-20, 13a-1, 13a-13, and 13b2-1. By engaging in the conduct described above, Gruntal willfully aided, abetted, and caused Gruntal Financial's violations of Section 13(a), 13(b) (2) (A), and 13(b) (5) and Rules 12b-20, 13a-1, 13a-13, and 13b2-1.

C. GRUNTAL'S VIOLATIONS OF BROKER-DEALER REPORTING AND RECORD-KEEPING PROVISIONS

Section 17(a) of the Exchange Act and Rules 17a-3 and 17a-4 thereunder require registered broker-dealers to make and keep certain books and records. The requirement that certain books and records be made also requires that those records be made accurately. U.S. v. Sloan, 389 F. Supp. 526, 528 (S.D.N.Y. 1975); In the Matter of Michael Alan Pettis, Exchange Act Release No. 33254 (Nov. 29, 1993). Rule 17a-11(d) requires a broker-dealer to notify the Commission and its principal self-regulatory organization the same day that it fails to meet the requirements of Rule 17a-3.

The Commission has emphasized the importance of the records maintained by broker-dealers pursuant to the Exchange Act, describing them as the "keystone of the surveillance of brokers and dealers by our staff and by the securities industry's self-regulatory bodies." Edward J. Mawod & Co., 46 SEC 865, 873 n.39 (1977), aff'd, 591 F.2d 588 (10th Cir. 1979).

Bao and Certain Senior Managers went to great lengths to hide their actions, including the intentional falsification of numerous books and records. Other books and records, although not intentionally falsified, were based upon information contained in the falsified records and therefore are also inaccurate. Books and records specifically required by Section 17(a) and Rule 17a-3, but which were falsified or inaccurate at Gruntal, include the following: (1) blotters containing an itemized daily record reflecting, among other things, all receipts and disbursements of cash and other debits and credits, and the account for which each such transaction was effected (17a-3(a)(1)); (2) ledgers reflecting all assets and liabilities, income and expense and capital accounts (17a-3(a)(2)); (3) ledger accounts itemizing separately as to each cash and margin account of every customer, among other things, all debits and credits to that account (17a-3(a)(3)); (4) ledgers reflecting dividends and interest received and securities failed to receive and failed to deliver (17a-3(a)(4)); (5) records with respect to each cash and margin account, indicating the name and address of the beneficial owner of such account (17a-3(a)(9)); and (6) a record of the proof of money balances of all ledger accounts in the form of trial balances (17a-3(a)(11)). Gruntal failed to give the Commission or the NYSE the lack of compliance notice required by Rule 17a-11(d).

Section 17(a) and (e) of the Exchange Act and Rule 17a-5(d) require registered broker-dealers to file with the Commission annual FOCUS reports. Section 17(a) and Rule 17a-5(a) require registered broker-dealers to file monthly and quarterly FOCUS reports on Form X-17A-5. Implicit in these provisions is the requirement that the information be accurate. See In the Matter of Nikko Sec. Co. Int'l, Exchange Act-Release No. 32331 (May 19, 1993). As a result of the diversions, Gruntal's annual FOCUS reports and monthly and quarterly FOCUS reports misstated Gruntal's income.

For the foregoing reasons, Gruntal willfully violated Section 17(a) and (e) and Rules 17a-3, 17a-4, 17a-5(a), 17a-5(d), and 17a-11(d) thereunder.

V.

Based on the foregoing, the Commission finds that:

- A. Gruntal Financial violated Section 17(a) of the Securities Act and Sections 10(b), 13(a), 13(b)(2)(A), and 13(b)(5) of the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-13, and 13b2-1 thereunder;

- B. Gruntal willfully violated Section 17(a) of the Securities Act and Sections 10(b), 15(c)(1), 17(a), and 17(e) of the Exchange Act and Rules 10b-5, 17a-3, 17a-4, 17a-5(a), 17a-5(d), and 17a-11(d) thereunder; and
- C. Gruntal willfully aided, abetted, and caused Gruntal Financial's violations of Section 17(a) of the Securities Act and Sections 10(b), 13(a), 13(b)(2)(A), and 13(b)(5) of the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-13, and 13b2-1 thereunder.

VI.

In view of the foregoing, it is in the public interest to impose the sanctions specified in the Offers of Settlement. In determining to accept the Offers, the Commission considered remedial acts undertaken by Gruntal and Gruntal Financial and cooperation afforded the Commission staff.

Accordingly, IT IS HEREBY ORDERED that:

- A. Gruntal be, and hereby is, censured;
- B. Gruntal, pursuant to Section 8A of the Securities Act and Section 21C of the Exchange Act, cease and desist from committing or causing any violation, and any future violation, of Section 17(a) of the Securities Act, Sections 10(b), 13(a), 13(b)(2)(A), 13(b)(5), 15(c)(1), 17(a), and 17(e) of the Exchange Act, and Rules 10b-5, 12b-20, 13a-1, 13a-13, 13b2-1, 17a-3, 17a-4, 17a-5(a), 17a-5(d), and 17a-11(d) thereunder;
- C. Gruntal Financial, pursuant to Section 8A of the Securities Act and Section 21C of the Exchange Act, cease and desist from committing or causing any violation, and any future violation, of Section 17(a) of the Securities Act, Sections 10(b), 13(a), 13(b)(2)(A), and 13(b)(5) of the Exchange Act, and Rules 10b-5, 12b-20, 13a-1, 13a-13, and 13b2-1 thereunder;
- D. Gruntal shall pay a civil money penalty in the amount of \$4 million pursuant to Section 21B of the Exchange Act. Such payment shall be: (1) made by United States postal money order, certified check, bank cashier's check, or bank money order; (2) made payable to the Securities and Exchange Commission; (3) hand-delivered, within 10 business days of the date of this Order, to the Comptroller, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549; and (4) submitted under cover letter identifying Gruntal as

a Respondent in these proceedings, and the Commission's case number (HO-2997), a copy of which shall be sent to Thomas C. Newkirk, Associate Director, Securities and Exchange Commission, 450 Fifth Street, N.W., Mail Stop 4-1, Washington D.C. 20549;

- E. Gruntal and Gruntal Financial (collectively "Respondents"), pursuant to Section 8A of the Securities Act and Sections 21B and 21C of the Exchange Act, shall pay an aggregate of \$5.5 million in disgorgement and prejudgment interest for the benefit of customers, states, and other third parties that are identified as due funds from Respondents as a result of the diversions of assets between 1984 and 1994 as described in this Order, in the manner set forth below;
- F. Respondents shall comply with the following undertakings:
1. To implement the above ordered disgorgement:
 - a. within ten business days of the date of this Order, Respondents shall deposit \$5.5 million in a Court Registry Investment System ("CRIS") account (the "Fund") to be established in accordance with the Commission's petition in the District Court pursuant to Section 20(c) of the Securities Act and Section 21(e) of the Exchange Act ("Petition");
 - b. within 30 days of the date of this Order, at Respondents' expense, Respondents shall retain the independent Fund Administrator ("Fund Administrator") appointed and approved by the District Court upon the Commission's recommendation and with the consent of the Respondents, which consent shall not be unreasonably withheld, who will:
 - i. have all appropriate powers and authority to perform his or her duties as set forth in this Order, including, without limitation, the powers to hire such persons as are reasonably necessary to perform his or her duties as set forth in this Order;
 - ii. file tax returns on behalf of the Fund;
 - iii. conduct such investigation, research, and review as is necessary and practicable to:
 - (A) verify Gruntal's representation to the Commission that it has repaid, recredited,

escheated, or properly segregated and scheduled for escheatment \$6.7 million which it has identified as escheatable, or presently believes to be escheatable, or has identified as belonging to customers, counterparties, vendors, and other third parties, in connection with the conduct described in this Order, and (B) where practical, identify the type (e.g., dividends), ownership (e.g., customer), and nature (e.g., escheatable) of the assets diverted in connection with the diversions of assets between 1984 and 1994 as described in this Order, which are presently so unidentified;

- iv. following such investigation and research, but in any event no later than one year after the date of this Order, submit to the District Court, the Director of the Division of Enforcement of the Commission, and Respondents: (A) a report of his or her findings, and (B) a Plan of Distribution to disburse the Fund in accordance with this Order;
 - v. after an opportunity for interested parties to be heard, and upon approval of the Plan of Distribution by the District Court, the Fund Administrator shall disburse the Fund in accordance with the Plan of Distribution;
 - vi. be entitled, to the extent that he or she deems appropriate, to rely upon work performed or to be performed by Ernst & Young LLP ("E&Y"), Deloitte & Touche LLP ("D&T"), Gruntal's Quality Assurance Task Force, Gruntal's Operations Division, and Gruntal's Operations Control Group; and
 - vii. be entitled, to the extent that he or she deems appropriate, to require Gruntal to continue the engagement of D&T and to maintain resources within its Operations Control Group to support the efforts of the Fund Administrator;
- c. in the event that the Fund Administrator determines, pursuant to Section VI.F.1.b.iii.(A) above, that Gruntal has not repaid, recredited, escheated, or properly segregated and scheduled for escheatment \$6.7 million in connection with the conduct described in this Order, Gruntal shall

disgorge into the Fund the difference between \$6.7 million and the amount the Fund Administrator determines that Gruntal has actually repaid, recredited, escheated, or properly segregated and scheduled for escheatment in connection with the conduct described in this Order. Such additional disgorgement shall be distributed pursuant to the terms of this Order that govern disbursements from the Fund;

- d. if, as a result of research by Respondents or by the Fund Administrator, any of the amount referred to in Section VI.F.1.b.iii.(A) above which is segregated and scheduled for escheatment is determined not to be escheatable and is determined to belong to customers, contra-parties, vendors, or other third parties, then Respondents shall pay such monies to the parties to whom they belong. If at any time any of the amount referred to in Section VI.F.1.b.iii.(A) above which is segregated and scheduled for escheatment is determined not to be escheatable and not to be owed to customers, contra-parties, vendors, or other third parties, then Respondents shall pay such monies into the Fund and such monies shall be disbursed pursuant to the terms of this Order that govern disbursements from the Fund;
- e. the Fund shall be used for the benefit of customers, contra-parties, vendors, states, and other third parties that are identified by the Fund Administrator as due funds from Respondents as a result of the diversions of assets between 1984 and 1994. The Fund is to be disbursed as follows:
 - i. first, to pay any taxes on the income earned on the Fund,
 - ii. second, to repay to customers such monies identified as owing to them,
 - iii. third, to repay to vendors, contra-parties, and other third parties such monies identified as owing to them,
 - iv. fourth, to escheat to the proper state(s) such monies identified as presently escheatable,
 - v. fifth, to have assets identified as potentially escheatable, but not yet ripe for

escheatment, properly maintained in segregated accounts until escheated, and

- vi. sixth, to pay any residual balance into the United States Treasury;
 - f. Respondents shall indemnify, defend, and hold harmless the Fund Administrator and his or her agents and attorneys from and against all liabilities, claims, and demands arising from or relating to any act or omission to act in the course of performing his or her duties, except to the extent that the District Court finds that such person acted in bad faith, gross negligence, reckless disregard of his or her duties, or in a manner that he or she knew was contrary to the terms of this Order; and
 - g. in the event that the Commission's Petition is not granted by the District Court, (i) any monies that would have been transferred to the CRIS account under control of the Fund Administrator and subject to the jurisdiction of the District Court shall instead be transferred to an appropriate account under the control of the Fund Administrator, subject to the jurisdiction of the Commission, (ii) the Fund Administrator shall be selected by the Commission with the consent of Respondents, which consent shall not be unreasonably withheld, and (iii) the Plan of Distribution proposed by the Fund Administrator shall be subject to approval by the Commission after an opportunity for interested parties to be heard; provided however, that if Respondents and the Commission agree, they may jointly move a United States District Court for approval and implementation of any such Plan of Distribution;
2. Respondents shall retain within 45 days of the date of this Order, at Respondents' expense, an Independent Consultant, acceptable to the Commission's staff, to:
- a. conduct a comprehensive review of Gruntal's policies and procedures concerning: (i) operations (back office), including but not limited to the cashier's department; (ii) the bank reconciliation department; (iii) the accounting department; (iv) dormant, abandoned, stale, unidentified, or escheatable assets; (v) suspense accounts, operations area accounts, and other accounts of a similar nature; (vi) the creation and maintenance

- of accurate books and records with respect to the foregoing; (vii) the internal audit department and functions; (viii) OTC trading; and (ix) compliance, in determining whether and to what extent there is a need for additional policies and procedures designed reasonably to prevent and detect, insofar as practicable, violations of the federal securities laws;
- b. conduct a comprehensive investigation of the facts and circumstances surrounding Gruntal's execution and reporting practices for OTC trades as described in this Order. Such investigation shall include, among other things: (i) the accuracy and timeliness of Gruntal's reporting of OTC trades and the manner in which Gruntal processed OTC market orders and OTC limit orders; (ii) the cause(s) of inaccurately or untimely reported OTC trades or improperly processed OTC trades; (iii) the persons responsible for the practices; (iv) the knowledge of management, if any, of the practices; (v) the financial harm to customers resulting from the practices; (vi) the identities of customers harmed; (vii) the amount by which each such customer was harmed; and (viii) the amount, if any, by which Gruntal was unjustly enriched as a result of such practices;
- c. review the policies and procedures that Gruntal has adopted and implemented since the activities described in this Order, to determine whether and to what extent there is a need for additional or amended policies and procedures designed reasonably to prevent and detect, insofar as practicable, violations of the federal securities laws;
- d. recommend policies and procedures (or amendments to existing policies and procedures) designed reasonably to prevent and detect, insofar as practicable, violations of the federal securities laws;
- e. be entitled, to the extent that he or she deems appropriate, to rely upon work performed or to be performed by E&Y, D&T, Gruntal's Quality Assurance Task Force, Gruntal's Operations Division, and Gruntal's Operations Control Group;
- f. be entitled, to the extent that he or she deems appropriate, to hire such persons as are reasonably necessary to perform his or her duties

as set forth in this Order, to require Gruntal to continue the engagement of D&T, and to require Gruntal to maintain resources within its Operations Control Group to support the efforts of the Independent Consultant;

- g. submit a written report to Gruntal's Board of Directors of his or her findings and recommendations, within six months of the date of this Order. Gruntal shall be provided a reasonable opportunity to comment on the Independent Consultant's review and recommendations;
- h. simultaneous with the submission of the written report referenced above to the Board of Directors of Gruntal, submit a copy of such report to the Director of the Division of Enforcement of the Commission and such other persons or entities as may be proposed by any governmental, regulatory, or self-regulatory body;
- i. conduct, on an annual basis for a period of three years commencing with the date of this Order, an audit of the policies and procedures described in Sections VI.F.2.a., c., and d. above, and the policies and procedures adopted pursuant to the Independent Consultant's recommendations, to ensure compliance with those procedures. As a result of such audit, the Independent Consultant may recommend new procedures or revisions to existing procedures, and to the system for applying such procedures, to achieve the objectives outlined in Sections VI.F.2.a., c., and d. above; and
- j. report to the Director of the Division of Enforcement of the Commission and Respondents:
 - (i) any material failure to comply with the procedures and system for applying those procedures, described in Sections VI.F.2.a., c., and d. above, and the policies and procedures adopted pursuant to the Independent Consultant's recommendations;
 - (ii) any other material failure by Respondents to comply with this Order; and
 - (iii) any violation of the federal securities laws;

3. Respondents shall adopt and implement, no later than 90 days after receipt of the Independent Consultant's report (or such other time as the Independent Consultant believes is necessary), such

policies and procedures as recommended by the Independent Consultant; provided however, that as to any of the Independent Consultant's recommendations that Gruntal determines is unduly burdensome and impractical, Gruntal may propose an alternative procedure reasonably designed to accomplish the same objectives. The Independent Consultant shall reasonably evaluate such alternative procedure and, if appropriate, either approve the alternative procedure, amend the recommendation, or reassert the original recommendation. Gruntal shall abide by the decision of the Independent Consultant and adopt and implement the alternative procedure, amended recommendation, or the original recommendation within the time period set by the Independent Consultant in light of the nature of the procedures;

4. Respondents shall pay to each customer identified by the Independent Consultant's report as having been financially harmed in connection with Gruntal's reporting or processing of OTC trades, within 90 days of the submission of the Independent Consultant's report to Gruntal's Board of Directors, an amount equal to the amount by which each such customer was harmed, plus accrued interest thereon calculated at the rate utilized by the Commission in cases involving disgorgement. If it is not possible or is impractical to make such payments to each customer harmed, then the monies not returned to customers shall be paid into the United States Treasury. In any event, Gruntal shall not retain the benefit of any monies improperly obtained in connection with the reporting or processing of OTC trades;

5. Respondents shall cooperate fully with the Fund Administrator and the Independent Consultant, including using all reasonable efforts to obtain the cooperation of Respondents' employees or other persons under their control, including E&Y and D&T, and giving the Fund Administrator and the Independent Consultant full access to all documents and premises under Respondents' control;

6. To ensure the independence of the Fund Administrator and the Independent Consultant, Respondents:

- a. shall not have the authority to terminate the Independent Consultant, or the Fund Administrator if selected by the Commission pursuant to Section VI.F.1.g. above, without the prior written

approval of the Director of the Division of Enforcement of the Commission;

- b. shall compensate the Fund Administrator, the Independent Consultant, and persons engaged to assist the Fund Administrator and Independent Consultant, for services rendered pursuant to this Order at their reasonable and customary rates;
- c. shall not, without the prior written consent of the Director of the Division of Enforcement of the Commission, enter into any legal, business, or other financial relationship with the Fund Administrator, Independent Consultant, any firm with which the foregoing are affiliated or of which they are a member, or any person engaged by the Fund Administrator or the Independent Consultant to assist the Fund Administrator or Independent Consultant in the performance of their duties under this Order, other than as described in this Order, during the period of their engagements and for a period of two years following the completion of their duties described in this Order; and
- d. shall not be in and shall not have an attorney-client relationship with the Fund Administrator or Independent Consultant and shall not seek to invoke the attorney-client or any other doctrine or privilege to prevent the Fund Administrator or Independent Consultant from transmitting any information, reports, or documents to the District Court, the Commission, or its staff;

7. If the Fund Administrator resigns or is otherwise unable to serve, a successor shall be appointed and approved by the District Court upon the Commission's recommendation and with the consent of the Respondents, which consent shall not be unreasonably withheld. Respondents shall retain such successor, at Respondents' expense, within 30 days after the successor's appointment and approval by the District Court. If the Fund Administrator is selected by the Commission pursuant to Section VI.F.1.g. above and resigns or is otherwise unable to serve, a successor shall be selected by the Commission with the consent of the Respondents, which consent shall not be unreasonably withheld. Respondents shall retain such successor, at Respondents' expense, within 30 days after the Commission's selection. If the Independent Consultant resigns or is otherwise unable to serve, Respondents shall retain a successor within 30 days, at

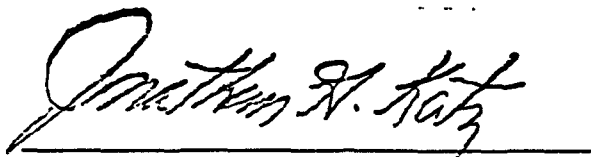
Respondents' expense, acceptable to the Commission's staff. All provisions in this Order that apply to the Fund Administrator or the Independent Consultant shall apply to any successor;

8. Gruntal shall maintain for a period of at least three years after the date of this Order a Committee of its Board of Directors (the "Committee"), consisting of no fewer than three persons, which shall: (a) review policy relating to the achievement of compliance with applicable federal securities laws and the rules and regulations of the Municipal Securities Rulemaking Board or of any national securities exchange or self-regulatory organization ("SRO") of which Gruntal is a member ("applicable rules and regulations"); (b) monitor Gruntal's implementation of any changes in Gruntal's policies and procedures adopted as a result of the Independent Consultant's review process described in Sections VI.F.2.a., c., and d. above; and (c) monitor Gruntal's efforts to detect, correct, and prevent failures to comply with applicable rules and regulations. The Committee shall require the General Counsel of Gruntal to submit quarterly to the Committee a written report which shall include a summary of: government and SRO investigations involving Gruntal or its employees; internal disciplinary actions; employee terminations for cause; and any material deficiencies in policies or procedures identified in any internal audit at Gruntal. In addition, the Committee shall provide a quarterly report to the Board of Directors of Gruntal, which shall include a summary of the activities of the Committee in ensuring the fulfillment of its responsibilities under this Order; and

9. Respondents shall cooperate, and use all reasonable efforts to cause its present or former officers, directors, agents, servants, employees, attorneys-in-fact, assigns, and all persons in active concert and participation with them to cooperate, with investigations, administrative proceedings, and litigation conducted by the Commission, other government agencies, securities exchanges, or SROs arising from or relating to the conduct described in this Order; and

G. Under no circumstances shall any of the assets referred to in Section VI. of this Order be paid to or revert to Respondents, their assigns, subsidiaries, or shareholder(s).

By the Commission.

A handwritten signature in cursive script, reading "Jonathan G. Katz", written over a horizontal line.

Jonathan G. Katz
Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 7279 / April 9, 1996

SECURITIES EXCHANGE ACT OF 1934
Release No. 37085 / April 9, 1996

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 771 / April 9, 1996

ADMINISTRATIVE PROCEEDING
File No. 3-8984

In the Matter of	:	
	:	
GRUNTAL & CO., INCORPORATED	:	ORDER INSTITUTING
	:	PUBLIC ADMINISTRATIVE
and	:	PROCEEDINGS, MAKING
	:	FINDINGS, IMPOSING
GRUNTAL FINANCIAL CORP.,	:	REMEDIAL SANCTIONS, AND
	:	ISSUING CEASE AND
Respondents.	:	DESIST ORDER
	:	

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be instituted against Gruntal & Co., Incorporated ("Gruntal") pursuant to Section 8A of the Securities Act of 1933 ("Securities Act") and Sections 15(b)(4) and 21C of the Securities Exchange Act of 1934 ("Exchange Act") and against Gruntal Financial Corp. ("Gruntal Financial") pursuant to Section 8A of the Securities Act and Section 21C of the Exchange Act. In anticipation of the institution of these administrative proceedings, Gruntal and Gruntal Financial have submitted Offers of Settlement, which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceeding brought by or on behalf of the Commission, or to which the Commission is a party, Gruntal and Gruntal Financial, by their Offers of Settlement, prior to a hearing pursuant to the Commission's Rules of Practice and without admitting or denying the findings set forth herein, consent to the entry of this Order Instituting Public Administrative Proceedings, Making Findings,

Imposing Remedial Sanctions, and Issuing Cease and Desist Order ("Order").

II.

Accordingly, IT IS HEREBY ORDERED that proceedings pursuant to Section 8A of the Securities Act and Sections 15(b)(4) and 21C of the Exchange Act be, and hereby are, instituted.

III.

The Commission makes the following findings:^{1/}

A. RESPONDENTS

1. Gruntal

At all times from December 15, 1983 to the present, Gruntal has been a broker-dealer registered with the Commission pursuant to Section 15(b) of the Exchange Act. Throughout that period, Gruntal has been a member of several national securities exchanges, including The New York Stock Exchange, Inc. ("NYSE"), and of the National Association of Securities Dealers, Inc. ("NASD"). As a broker-dealer, Gruntal provides a full range of securities brokerage and trading services, as well as related financial services.

From 1983 to June 1990, Gruntal conducted its back office operations through a wholly owned subsidiary, Regional Clearing Corp. ("Regional Clearing"). In June-1990, Regional Clearing was merged into Gruntal. As used in this Order, the term "Gruntal" refers, as the context requires, to Gruntal and/or Regional Clearing.

2. Gruntal Financial

From December 15, 1983 to the present, Gruntal Financial has been a Delaware corporation operating a securities brokerage business through Gruntal, its wholly owned subsidiary. For the period December 1983 to August 1987, Gruntal Financial was a publicly traded corporation with its securities registered pursuant to Section 12(b) of the Exchange Act and listed on the NYSE. From December 1983 to August 1987, Gruntal Financial was required to file periodic reports with the Commission pursuant to Section 13 of the Exchange Act. In June 1986, Gruntal Financial

^{1/} The findings herein and the entry of this Order are solely for the purposes of this proceeding and shall not be binding on any other person or entity named in any other proceeding.

conducted an offering of 7 1/2% Convertible Subordinated Debentures due 2011.

In August 1987, Gruntal Financial was acquired by The Home Group, Inc., a public corporation whose securities were registered pursuant to Section 12(b) of the Exchange Act. Gruntal Financial was held as a subsidiary of The Home Insurance Company, a wholly owned subsidiary of The Home Group, Inc. In May 1989, The Home Group, Inc. changed its name to AmBase Corporation. In February 1991, The Home Insurance Company was acquired by Home Holdings Inc., a public corporation with its securities registered pursuant to Section 12(b) of the Exchange Act. Home Holdings Inc. went private in mid-1995.

B. OTHER RELEVANT PERSON

Edward E. Bao

Edward E. Bao was Gruntal's Executive Vice President for Operations and Administration. Bao also held the same position at Gruntal Financial. Bao's employment at Gruntal and Gruntal Financial was terminated on December 16, 1994.

C. SUMMARY

This proceeding involves conduct in two areas. The first, and principal, area involves violations of the antifraud, reporting, and record-keeping provisions of the federal securities laws in connection with three separate schemes to divert assets that occurred between 1984 and 1994 and that were instituted by certain members of Gruntal senior management (who left the firm subsequent to the conduct discussed herein). In those schemes, securities and funds totalling over \$11 million were diverted intentionally from customer accounts, dividend "overages,"^{2/} customer and vendor checks, and other sources at Gruntal. Approximately \$5 million of the diverted assets were moved to fictitious customer accounts and then transferred to

^{2/} Dividend "overages" resulted at Gruntal when the firm received stock dividends, cash dividends, or interest accrued on debt securities from issuing corporations in excess of those that its books showed were due to customer or proprietary accounts. See Edward C. Jaegerman, 46 SEC 706, 708 (1976). For example, Gruntal received such dividends when its customers sold securities between their record dates and their payment dates. Those dividends did not belong to Gruntal; instead, Gruntal held them as a "debtor," with a "duty" to transmit the unclaimed dividends to their beneficial owners. See Delaware v. New York, 113 S. Ct. 1550, 1559 (1993).

Gruntal profit and loss ("P&L") accounts or used to make off-books payments of Gruntal expenses. Thus, Gruntal used these diverted assets artificially to inflate its income or reduce its expenses. The remaining \$6 million of the diverted assets were embezzled by certain members of Gruntal management implementing the schemes.

In furtherance of these schemes, the Gruntal officers and managers implementing the diversions falsified Gruntal's books and records. To carry out and conceal the diversions, they created fictitious customer accounts. Other books and records, although not intentionally falsified, were based upon information contained in the falsified records and therefore were inaccurate. The diversions were instituted originally to inflate Gruntal's income. As a result of the diversions, Gruntal filed periodic FOCUS reports that overstated firm income, and Gruntal Financial filed periodic reports that mischaracterized the diverted assets and misstated Gruntal Financial's income. These reports also failed to disclose the diversion of customer and other third party funds to income and the involvement of certain officers and managers in those activities.

The second area involves Gruntal's execution and reporting of certain Over-the-Counter ("OTC") trades. In mid-1995, NASD reports indicated that Gruntal's late reported OTC trades exceeded the industry average. Gruntal subsequently reviewed a sample of such trades and found that, in a limited number of instances, customers were financially disadvantaged in connection with these practices.

D. THE MISAPPROPRIATION SCHEMES

1. Gruntal Misappropriates Assets to Increase Its Income

a. Sources of Diverted Assets

Beginning in 1984, Bao and certain senior managers under his control identified various assets that could be diverted and, ultimately, misappropriated for Gruntal's benefit. At Bao's direction, this process was conducted initially by three members of Gruntal's senior management: its Director of Operations, its Manager of Internal Audit, and the Executive Cashier (hereinafter "Certain Senior Managers").^{3/} By 1984, these managers realized

^{3/} The misappropriation schemes came to light after the Executive Cashier's sudden, unexpected death on October 16, 1994. In November 1994, Gruntal terminated the employment of the Director of Operations and the Manager of Internal Audit. Both of those individuals subsequently have pleaded guilty to a two-count (continued...)

that hundreds of thousands of dollars worth of overages had accrued in Gruntal dividend payable accounts.^{4/} At the behest of Bao -- the number two officer at Gruntal -- Certain Senior Managers undertook to ascertain to whom the overages belonged and the likelihood that Gruntal might yet receive claims for them. Overages that were unlikely to be claimed became candidates for diversion.

The overages were potentially escheatable property. Thus, if they had remained unclaimed, Gruntal should have eventually escheated them to the states. Instead, Bao and Certain Senior Managers diverted unclaimed overages out of the dividend accounts.

In about 1987 or 1988, Bao and Certain Senior Managers realized that Gruntal's bank reconciliation accounts held stale or outstanding customer and vendor checks that Gruntal could misappropriate. Gruntal's normal procedures required it to notify its customers of the checks. If the checks remained unclaimed after such notification, Gruntal was required eventually to pay them to the appropriate states. Gruntal did abide by these procedures for checks of smaller denominations; however, larger checks were diverted out of the bank reconciliation accounts.^{5/}

In addition, Gruntal, acting through Bao and Certain Senior Managers, diverted assets from dormant customer accounts. Securities and customer money balances were transferred out of customer accounts that were inactive or for which mailed account statements had been returned.

b. Fictitious Accounts and Falsified Records Hide the Diverted Assets

Beginning in 1984, Bao and Certain Senior Managers opened securities accounts at Gruntal under fictitious customer names.

^{3/}(...continued)

criminal information filed by the United States Attorney's Office for the Southern District of New York.

^{4/} Gruntal used these accounts to receive, hold, and disburse the stock dividends, cash dividends, and accrued interest that it received from issuing corporations.

^{5/} Notification of customers who had "stale" checks was more than a mere pro forma procedure. In many cases, these checks did belong to present, living customers. In fact, during the course of the diversions, Certain Senior Managers were forced to re-credit to customers over \$700,000 for previously diverted checks when customers contacted Gruntal inquiring about their money.

These accounts were given numbers purporting to identify them as customer accounts. From 1984 and continuing for a decade, dividend overages, stale checks, and other assets targeted for diversion were transferred into these fictitious customer accounts. To avoid detection and to obscure the true nature of the assets, these transfers often were made by means of complex, multiple-step transactions that utilized otherwise legitimate Gruntal operational or suspense accounts as interim stopping points. From fictitious customer accounts, diverted assets were transferred into the firm's P&L accounts and falsely credited as income.^{6/} These transfers tended to coincide with downturns in Gruntal's monthly income. Sometimes the diverted assets were used to make off-books payments of firm expenses, thereby reducing Gruntal's liabilities.

In carrying out the scheme, Gruntal, acting through Bao and Certain Senior Managers, created, or caused to be created, numerous fictitious and false books and records, including account opening documents, account statement entries, debit and credit memos, dividend claim forms, and accounting and journal entries.^{7/} In addition, to avoid detection, Bao and Certain Senior Managers periodically closed the fictitious customer accounts and opened new accounts to take their place, utilizing a number of fictitious accounts over time. Finally, Gruntal, through Bao and Certain Senior Managers, circumvented and disregarded certain procedures and internal controls, in particular those relating to opening new accounts and the proper handling of abandoned and/or escheatable property.

2. Embezzlement of Diverted Assets

a. Certain Senior Managers Divert Assets for Their Own Benefit

In about 1987, Certain Senior Managers began to divert assets for their own benefit. Their scheme drew on the same sources of assets utilized in the original diversions and largely used the same methods for diverting those assets. For their scheme also, Certain Senior Managers created, or caused to be created, fictitious or false records. However, this second

^{6/} In some instances, the diversions bypassed the fictitious customer accounts, and items were moved from their sources to operational or suspense accounts and from those accounts directly to Gruntal's P&L.

^{7/} The implementation and concealment of the scheme was effectively assisted -- knowingly, recklessly, or inadvertently -- by individuals from several departments at Gruntal, including bank reconciliation, abandoned property, internal audit, accounting, and the back office.

scheme largely avoided the fictitious customer accounts, and the assets diverted under this scheme ultimately left the firm -- without the authorization of other officers at Gruntal.

b. Executive Cashier Diverts Assets for His Own Use

A third diversion scheme developed when the Executive Cashier began an embezzlement on his own behalf. The Executive Cashier implemented a scheme based primarily on the creation of debits in Gruntal's reorganization account and which ultimately involved the creation, in some instances, of false "fails to deliver."^{8/} He then directed the alteration and falsification of Gruntal's corresponding records. Only a small portion of the assets the Executive Cashier embezzled came from the sources of assets used in the other diversion schemes. The Executive Cashier's scheme was conducted without the authorization of other officers at Gruntal.

E. FALSE FILINGS

1. Gruntal Financial

From 1985 through mid-1987, Gruntal Financial filed with the Commission false and misleading periodic reports and a false and misleading registration statement. Those reports, including the financial statements contained therein, were misstated because they failed to reflect, disclose, or correctly characterize the amounts and uses of the diverted assets. As a result, Gruntal Financial's income was overstated. Because a large number of Gruntal Financial's books and records were falsified, it is not always possible to quantify the precise impact of the diversions on income during this period. Nevertheless, for some periods, the misstatement of income can be clearly ascertained. For example, as a result of the diversions, Gruntal Financial's annual report on Form 10-K for fiscal year 1985 overstated its pre-tax income by approximately 15%. In addition, Gruntal Financial's periodic reports and registration statement failed to disclose the diversion of customer and other third party funds to income and management's role in those activities.

The false and misleading Gruntal Financial filings include:

^{8/} A fail to deliver occurs when the selling broker-dealer, in this case Gruntal, has failed to deliver securities to the buying broker-dealer. The selling broker-dealer will not receive payment as long as the fail continues. Thus, the creation of a false fail to deliver created the appearance that monies actually missing were merely monies that were owed to, and had not yet been received by, Gruntal.

(1) A registration statement on Form S-1, filed on June 2, 1986, and Amendment No. 1 thereto, filed on June 18, 1986, both filed in connection with Gruntal Financial's offering of 7 1/2% Convertible Subordinated Debentures due June 15, 2011;

(2) Annual reports on Form 10-K for the years 1985 and 1986; and

(3) A quarterly report on Form 10-Q for the third quarter of fiscal year 1987.

2. Gruntal

Between 1985 and 1994, Gruntal filed false and misleading FOCUS reports with the Commission and with the NYSE. These reports, including the income statements contained therein, overstated Gruntal's income. Because Bao and Certain Senior Managers falsified a large number of Gruntal's books and records, it is not always possible to quantify the precise impact of the diversions on the firm's income during this period. Nevertheless, for some periods, the misstatement can be clearly ascertained. For example, by diverting assets to income, Gruntal falsely overstated its pre-tax income by approximately 13% on its 1985 annual FOCUS report. Similarly, Gruntal's quarterly FOCUS report on Form X-17A-5 for the quarter ended June 28, 1991, overstated pre-tax income by approximately 130%.

The false Gruntal filings include:

(1) Annual FOCUS reports for fiscal years 1985 through 1994;

(2) Certain quarterly FOCUS reports on Form X-17A-5 from second quarter 1986 through fourth quarter 1994; and

(3) Certain monthly FOCUS reports on Form X-17A-5 for months from April 1986 through October 1994.

F. LATE REPORTING AND ORDER EXECUTION PRACTICES

In mid-1995, NASD reports issued to Gruntal indicated that Gruntal's late reported OTC trades exceeded the industry average. In November 1995, Gruntal undertook a study aimed at finding the reasons for the late reported trades. As part of that study, Gruntal examined a random sample of those trades. Gruntal found that, in a limited number of instances, customers had been financially disadvantaged by Gruntal's trading practices. For example, Gruntal identified two instances in which a customer placed an order to buy a particular OTC stock, but the order was not executed in a timely manner. Gruntal's trading desk, which had started the day flat with regard to that particular stock, subsequently built a position in it. Once that position was

built, the customer's order was filled from the position, to the customer's detriment. Gruntal has repaid those disadvantaged customers that it has identified to date.

A broker-dealer which fails to transmit promptly information required by an effective transaction reporting plan with respect to a reported security violates Section 11A(a)(2) of the Exchange Act and Rule 11Aa3-1(c) thereunder. A broker-dealer which fails to execute a customer's order promptly in accordance with the customer's instructions without disclosure violates the antifraud provisions, including Sections 10(b) and 15(c) of the Exchange Act and Rules 10b-5 and 15c2-1 thereunder and Section 17(a) of the Securities Act. As set forth below in Section VI.F.2. of this Order, an Independent Consultant acceptable to the Commission's staff will investigate the OTC order execution and reporting practices set forth above and, among other things, will direct Gruntal to reimburse any customers who have been financially harmed in connection with Gruntal's processing of OTC trades.

IV.

A. VIOLATIONS OF THE ANTIFRAUD PROVISIONS

Section 17(a) of the Securities Act proscribes fraud in connection with the "offer or sale" of securities. Section 10(b) of the Exchange Act and Rule 10b-5 thereunder prohibit fraud in connection with the purchase or sale of a security. Section 15(c)(1) of the Exchange Act prohibits a broker-dealer from effecting transactions in securities, otherwise than on a national securities exchange of which it is a member, by means of any manipulative, deceptive, or fraudulent device or contrivance.

A broker-dealer is entrusted with the funds and securities of its customers. Customers rely upon their brokerage. But, from 1984 through 1994, Bao and Certain Senior Managers took assets in the form of customer securities and balances, stale customer and vendor checks, and unclaimed dividends. They took pains to hide their actions.

A broker-dealer's misappropriation of customer securities is a violation of the antifraud provisions of the federal securities laws. Donald T. Sheldon, 51 SEC 59, 62-63 & n.11 (1992), aff'd, 45 F.3d 1515 (11th Cir. 1995). "[I]t is a fraudulent and deceptive act, practice, and course of business, which operates as a fraud and deceit on a customer, for a broker-dealer to . . . convert to his own use customers' funds or fully-paid for securities of customers held by the broker-dealer for safe-keeping." Sheldon, 51 SEC at 62 n.10 (quoting Ezra Weiss, Registration and Regulation of Brokers and Dealers 181 (1965)). At Gruntal, a substantial amount of customer funds and securities

were converted for the broker-dealer's use. Gruntal also violated the antifraud provisions when it misappropriated unclaimed dividend overages held in its dividend accounts and converted the dividends for firm use. Edward C. Jaegerman, 46 SEC 706, 708-09 (1976).

The "in connection with" requirement of the antifraud provisions "is met if the fraud alleged 'somehow touches upon' or has 'some nexus' with 'any securities transaction.'" SEC v. Rana Research, Inc., 8 F.3d 1358, 1362 (9th Cir. 1993) (quoting SEC v. Clark, 915 F.2d 439, 449 (9th Cir. 1990)).^{9/} Transactions in securities were integral to the fraudulent activities at Gruntal. Gruntal officers and managers removed balances and securities from customers' securities accounts, purchased securities with the stolen balances, sold customers' securities, took customer checks representing proceeds of securities transactions, and misappropriated dividends payable to contra-brokers, institutional investors, and Gruntal's customers.

To violate Section 17(a)(1), Section 10(b), or Rule 10b-5, a defendant must act with scienter. Aaron v. SEC, 446 U.S. 680, 701-02 (1980). Bao and Certain Senior Managers at Gruntal and Gruntal Financial knowingly instituted and condoned the diversions. Gruntal and Gruntal Financial are chargeable with their employees' state of mind. See SEC v. Manor Nursing Ctrs., Inc., 458 F.2d 1082, 1089 n.3 (2d Cir. 1972).

From 1985 through mid-1987, Gruntal Financial itself violated the antifraud provisions by filing certain materially false and misleading reports. Gruntal Financial was a holding company conducting its business through Gruntal. The original diversion scheme was instituted by Gruntal to inflate its income. As a result of Gruntal's overstated income, Gruntal Financial's income was also inflated, and Gruntal Financial filed with the Commission periodic reports and a registration statement that were materially misstated -- mischaracterizing the diverted assets and overstating income.^{10/} Gruntal Financial's filings were also made materially misleading by their failure to disclose

^{9/} Although the courts are in some disagreement over the contours of the "in connection with" requirement for a private plaintiff, "its meaning in SEC actions remains as broad and flexible as is necessary to accomplish the statute's purpose of protecting investors." Rana Research, 8 F.3d at 1362 (discussing requirement in context of case brought under Section 10(b)).

^{10/} A fact is material if there is a substantial likelihood that a reasonable investor would consider the information to be important. Basic Inc. v. Levinson, 485 U.S. 224, 231-32 (1988). Information regarding a company's income is among the most important information for making an investment decision.

the diversions at Gruntal or the involvement of certain members of senior management. See SEC v. Kalvex Inc., 425 F. Supp. 310, 315-16 (S.D.N.Y. 1975); cf. SEC v. Scott, 565 F. Supp. 1513, 1527 (S.D.N.Y. 1983) (stating that failure to disclose kickback scheme involving principal obviously material), aff'd sub nom. SEC v. Cayman Islands Reinsurance Corp., 734 F.2d 118 (2d Cir. 1984). During this period, Gruntal Financial securities were listed and traded on the NYSE, and, in June 1986, Gruntal Financial conducted an offering of Convertible Subordinated Debentures.

In order to establish liability for aiding and abetting, the Commission must establish (1) the existence of a primary violation, (2) that the aider or abettor had a general awareness that his role was part of an overall activity that was improper, and (3) that the aider or abettor knowingly and substantially assisted the principal violation. Dominick & Dominick, Inc., 50 SEC 571, 577 (1991).

Gruntal willfully aided, abetted, and caused Gruntal Financial's violations of the antifraud provisions. Gruntal, acting through Bao and Certain Senior Managers, knowingly implemented and condoned a scheme by which assets were transferred fraudulently and Gruntal's income was artificially inflated. As a result of that scheme, Gruntal Financial filed with the Commission materially misstated reports.

For the foregoing reasons, Gruntal willfully violated Section 17(a) of the Securities Act, Sections 10(b) and 15(c)(1) of the Exchange Act, and Rule 10b-5 thereunder by fraudulent transactions and practices, and Gruntal Financial violated Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder by material misrepresentations and omissions in its periodic reports and registration statement. Moreover, Gruntal willfully aided, abetted, and caused Gruntal Financial's violations.

B. GRUNTAL FINANCIAL'S VIOLATIONS OF EXCHANGE ACT REPORTING AND RECORD-KEEPING PROVISIONS

Section 13(a) of the Exchange Act and Rules 13a-1 and 13a-13 thereunder require issuers with securities registered under Section 12 of the Exchange Act to file annual and quarterly reports with the Commission and to keep this information current. The obligation to file such reports embodies the requirement that they be true and correct. See, e.g., SEC v. Savoy Indus., Inc., 587 F.2d 1149, 1165 (D.C. Cir. 1978), cert. denied, 440 U.S. 913 (1979). Exchange Act Rule 12b-20 further requires the inclusion of any additional material information that is necessary to make required statements, in light of the circumstances under which they were made, not misleading. Information regarding the

financial condition of a company is presumptively material. SEC v. Blavin, 760 F.2d 706, 711 (6th Cir. 1985).

As discussed above, from 1985 through mid-1987 Gruntal Financial filed certain false and misleading periodic reports with the Commission that mischaracterized the diverted assets, misstated Gruntal Financial's income, and failed to disclose management's role in the diversion of customer and other third party funds to income.

Section 13(b) (2) (A) of the Exchange Act requires Section 12 registrants to make and keep books, records, and accounts accurately reflecting transactions involving their assets. Section 13(b) (5) of the Exchange Act provides that no person shall knowingly falsify any such book, record, or account or circumvent internal controls. Rule 13b2-1 also prohibits the falsification of any book, record, or account subject to Section 13(b) (2) (A).

From 1984 through mid-1987, Gruntal Financial's books and records reflecting transactions in its assets were not merely inaccurate, they were intentionally falsified. Its internal accounting controls were intentionally circumvented.

For the foregoing reasons, Gruntal Financial violated Section 13(a), 13(b) (2) (A), and 13(b) (5) and Rules 12b-20, 13a-1, 13a-13, and 13b2-1. By engaging in the conduct described above, Gruntal willfully aided, abetted, and caused Gruntal Financial's violations of Section 13(a), 13(b) (2) (A), and 13(b) (5) and Rules 12b-20, 13a-1, 13a-13, and 13b2-1.

C. GRUNTAL'S VIOLATIONS OF BROKER-DEALER REPORTING AND RECORD-KEEPING PROVISIONS

Section 17(a) of the Exchange Act and Rules 17a-3 and 17a-4 thereunder require registered broker-dealers to make and keep certain books and records. The requirement that certain books and records be made also requires that those records be made accurately. U.S. v. Sloan, 389 F. Supp. 526, 528 (S.D.N.Y. 1975); In the Matter of Michael Alan Pettis, Exchange Act Release No. 33254 (Nov. 29, 1993). Rule 17a-11(d) requires a broker-dealer to notify the Commission and its principal self-regulatory organization the same day that it fails to meet the requirements of Rule 17a-3.

The Commission has emphasized the importance of the records maintained by broker-dealers pursuant to the Exchange Act, describing them as the "keystone of the surveillance of brokers and dealers by our staff and by the securities industry's self-regulatory bodies." Edward J. Mawod & Co., 46 SEC 865, 873 n.39 (1977), aff'd, 591 F.2d 588 (10th Cir. 1979).

Bao and Certain Senior Managers went to great lengths to hide their actions, including the intentional falsification of numerous books and records. Other books and records, although not intentionally falsified, were based upon information contained in the falsified records and therefore are also inaccurate. Books and records specifically required by Section 17(a) and Rule 17a-3, but which were falsified or inaccurate at Gruntal, include the following: (1) blotters containing an itemized daily record reflecting, among other things, all receipts and disbursements of cash and other debits and credits, and the account for which each such transaction was effected (17a-3(a)(1)); (2) ledgers reflecting all assets and liabilities, income and expense and capital accounts (17a-3(a)(2)); (3) ledger accounts itemizing separately as to each cash and margin account of every customer, among other things, all debits and credits to that account (17a-3(a)(3)); (4) ledgers reflecting dividends and interest received and securities failed to receive and failed to deliver (17a-3(a)(4)); (5) records with respect to each cash and margin account, indicating the name and address of the beneficial owner of such account (17a-3(a)(9)); and (6) a record of the proof of money balances of all ledger accounts in the form of trial balances (17a-3(a)(11)). Gruntal failed to give the Commission or the NYSE the lack of compliance notice required by Rule 17a-11(d).

Section 17(a) and (e) of the Exchange Act and Rule 17a-5(d) require registered broker-dealers to file with the Commission annual FOCUS reports. Section 17(a) and Rule 17a-5(a) require registered broker-dealers to file monthly and quarterly FOCUS reports on Form X-17A-5. Implicit in these provisions is the requirement that the information be accurate. See In the Matter of Nikko Sec. Co. Int'l, Exchange Act-Release No. 32331 (May 19, 1993). As a result of the diversions, Gruntal's annual FOCUS reports and monthly and quarterly FOCUS reports misstated Gruntal's income.

For the foregoing reasons, Gruntal willfully violated Section 17(a) and (e) and Rules 17a-3, 17a-4, 17a-5(a), 17a-5(d), and 17a-11(d) thereunder.

V.

Based on the foregoing, the Commission finds that:

- A. Gruntal Financial violated Section 17(a) of the Securities Act and Sections 10(b), 13(a), 13(b)(2)(A), and 13(b)(5) of the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-13, and 13b2-1 thereunder;

- B. Gruntal willfully violated Section 17(a) of the Securities Act and Sections 10(b), 15(c)(1), 17(a), and 17(e) of the Exchange Act and Rules 10b-5, 17a-3, 17a-4, 17a-5(a), 17a-5(d), and 17a-11(d) thereunder; and
- C. Gruntal willfully aided, abetted, and caused Gruntal Financial's violations of Section 17(a) of the Securities Act and Sections 10(b), 13(a), 13(b)(2)(A), and 13(b)(5) of the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-13, and 13b2-1 thereunder.

VI.

In view of the foregoing, it is in the public interest to impose the sanctions specified in the Offers of Settlement. In determining to accept the Offers, the Commission considered remedial acts undertaken by Gruntal and Gruntal Financial and cooperation afforded the Commission staff.

Accordingly, IT IS HEREBY ORDERED that:

- A. Gruntal be, and hereby is, censured;
- B. Gruntal, pursuant to Section 8A of the Securities Act and Section 21C of the Exchange Act, cease and desist from committing or causing any violation, and any future violation, of Section 17(a) of the Securities Act, Sections 10(b), 13(a), 13(b)(2)(A), 13(b)(5), 15(c)(1), 17(a), and 17(e) of the Exchange Act, and Rules 10b-5, 12b-20, 13a-1, 13a-13, 13b2-1, 17a-3, 17a-4, 17a-5(a), 17a-5(d), and 17a-11(d) thereunder;
- C. Gruntal Financial, pursuant to Section 8A of the Securities Act and Section 21C of the Exchange Act, cease and desist from committing or causing any violation, and any future violation, of Section 17(a) of the Securities Act, Sections 10(b), 13(a), 13(b)(2)(A), and 13(b)(5) of the Exchange Act, and Rules 10b-5, 12b-20, 13a-1, 13a-13, and 13b2-1 thereunder;
- D. Gruntal shall pay a civil money penalty in the amount of \$4 million pursuant to Section 21B of the Exchange Act. Such payment shall be: (1) made by United States postal money order, certified check, bank cashier's check, or bank money order; (2) made payable to the Securities and Exchange Commission; (3) hand-delivered, within 10 business days of the date of this Order, to the Comptroller, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549; and (4) submitted under cover letter identifying Gruntal as

a Respondent in these proceedings, and the Commission's case number (HO-2997), a copy of which shall be sent to Thomas C. Newkirk, Associate Director, Securities and Exchange Commission, 450 Fifth Street, N.W., Mail Stop 4-1, Washington D.C. 20549;

- E. Gruntal and Gruntal Financial (collectively "Respondents"), pursuant to Section 8A of the Securities Act and Sections 21B and 21C of the Exchange Act, shall pay an aggregate of \$5.5 million in disgorgement and prejudgment interest for the benefit of customers, states, and other third parties that are identified as due funds from Respondents as a result of the diversions of assets between 1984 and 1994 as described in this Order, in the manner set forth below;
- F. Respondents shall comply with the following undertakings:
1. To implement the above ordered disgorgement:
 - a. within ten business days of the date of this Order, Respondents shall deposit \$5.5 million in a Court Registry Investment System ("CRIS") account (the "Fund") to be established in accordance with the Commission's petition in the District Court pursuant to Section 20(c) of the Securities Act and Section 21(e) of the Exchange Act ("Petition");
 - b. within 30 days of the date of this Order, at Respondents' expense, Respondents shall retain the independent Fund Administrator ("Fund Administrator") appointed and approved by the District Court upon the Commission's recommendation and with the consent of the Respondents, which consent shall not be unreasonably withheld, who will:
 - i. have all appropriate powers and authority to perform his or her duties as set forth in this Order, including, without limitation, the powers to hire such persons as are reasonably necessary to perform his or her duties as set forth in this Order;
 - ii. file tax returns on behalf of the Fund;
 - iii. conduct such investigation, research, and review as is necessary and practicable to:
 - (A) verify Gruntal's representation to the Commission that it has repaid, recredited,

escheated, or properly segregated and scheduled for escheatment \$6.7 million which it has identified as escheatable, or presently believes to be escheatable, or has identified as belonging to customers, counterparties, vendors, and other third parties, in connection with the conduct described in this Order, and (B) where practical, identify the type (e.g., dividends), ownership (e.g., customer), and nature (e.g., escheatable) of the assets diverted in connection with the diversions of assets between 1984 and 1994 as described in this Order, which are presently so unidentified;

- iv. following such investigation and research, but in any event no later than one year after the date of this Order, submit to the District Court, the Director of the Division of Enforcement of the Commission, and Respondents: (A) a report of his or her findings, and (B) a Plan of Distribution to disburse the Fund in accordance with this Order;
 - v. after an opportunity for interested parties to be heard, and upon approval of the Plan of Distribution by the District Court, the Fund Administrator shall disburse the Fund in accordance with the Plan of Distribution;
 - vi. be entitled, to the extent that he or she deems appropriate, to rely upon work performed or to be performed by Ernst & Young LLP ("E&Y"), Deloitte & Touche LLP ("D&T"), Gruntal's Quality Assurance Task Force, Gruntal's Operations Division, and Gruntal's Operations Control Group; and
 - vii. be entitled, to the extent that he or she deems appropriate, to require Gruntal to continue the engagement of D&T and to maintain resources within its Operations Control Group to support the efforts of the Fund Administrator;
- c. in the event that the Fund Administrator determines, pursuant to Section VI.F.1.b.iii.(A) above, that Gruntal has not repaid, recredited, escheated, or properly segregated and scheduled for escheatment \$6.7 million in connection with the conduct described in this Order, Gruntal shall

disgorge into the Fund the difference between \$6.7 million and the amount the Fund Administrator determines that Gruntal has actually repaid, recredited, escheated, or properly segregated and scheduled for escheatment in connection with the conduct described in this Order. Such additional disgorgement shall be distributed pursuant to the terms of this Order that govern disbursements from the Fund;

- d. if, as a result of research by Respondents or by the Fund Administrator, any of the amount referred to in Section VI.F.1.b.iii.(A) above which is segregated and scheduled for escheatment is determined not to be escheatable and is determined to belong to customers, contra-parties, vendors, or other third parties, then Respondents shall pay such monies to the parties to whom they belong. If at any time any of the amount referred to in Section VI.F.1.b.iii.(A) above which is segregated and scheduled for escheatment is determined not to be escheatable and not to be owed to customers, contra-parties, vendors, or other third parties, then Respondents shall pay such monies into the Fund and such monies shall be disbursed pursuant to the terms of this Order that govern disbursements from the Fund;
- e. the Fund shall be used for the benefit of customers, contra-parties, vendors, states, and other third parties that are identified by the Fund Administrator as due funds from Respondents as a result of the diversions of assets between 1984 and 1994. The Fund is to be disbursed as follows:
 - i. first, to pay any taxes on the income earned on the Fund,
 - ii. second, to repay to customers such monies identified as owing to them,
 - iii. third, to repay to vendors, contra-parties, and other third parties such monies identified as owing to them,
 - iv. fourth, to escheat to the proper state(s) such monies identified as presently escheatable,
 - v. fifth, to have assets identified as potentially escheatable, but not yet ripe for

escheatment, properly maintained in segregated accounts until escheated, and

- vi. sixth, to pay any residual balance into the United States Treasury;
 - f. Respondents shall indemnify, defend, and hold harmless the Fund Administrator and his or her agents and attorneys from and against all liabilities, claims, and demands arising from or relating to any act or omission to act in the course of performing his or her duties, except to the extent that the District Court finds that such person acted in bad faith, gross negligence, reckless disregard of his or her duties, or in a manner that he or she knew was contrary to the terms of this Order; and
 - g. in the event that the Commission's Petition is not granted by the District Court, (i) any monies that would have been transferred to the CRIS account under control of the Fund Administrator and subject to the jurisdiction of the District Court shall instead be transferred to an appropriate account under the control of the Fund Administrator, subject to the jurisdiction of the Commission, (ii) the Fund Administrator shall be selected by the Commission with the consent of Respondents, which consent shall not be unreasonably withheld, and (iii) the Plan of Distribution proposed by the Fund Administrator shall be subject to approval by the Commission after an opportunity for interested parties to be heard; provided however, that if Respondents and the Commission agree, they may jointly move a United States District Court for approval and implementation of any such Plan of Distribution;
2. Respondents shall retain within 45 days of the date of this Order, at Respondents' expense, an Independent Consultant, acceptable to the Commission's staff, to:
- a. conduct a comprehensive review of Gruntal's policies and procedures concerning: (i) operations (back office), including but not limited to the cashier's department; (ii) the bank reconciliation department; (iii) the accounting department; (iv) dormant, abandoned, stale, unidentified, or escheatable assets; (v) suspense accounts, operations area accounts, and other accounts of a similar nature; (vi) the creation and maintenance

- of accurate books and records with respect to the foregoing; (vii) the internal audit department and functions; (viii) OTC trading; and (ix) compliance, in determining whether and to what extent there is a need for additional policies and procedures designed reasonably to prevent and detect, insofar as practicable, violations of the federal securities laws;
- b. conduct a comprehensive investigation of the facts and circumstances surrounding Gruntal's execution and reporting practices for OTC trades as described in this Order. Such investigation shall include, among other things: (i) the accuracy and timeliness of Gruntal's reporting of OTC trades and the manner in which Gruntal processed OTC market orders and OTC limit orders; (ii) the cause(s) of inaccurately or untimely reported OTC trades or improperly processed OTC trades; (iii) the persons responsible for the practices; (iv) the knowledge of management, if any, of the practices; (v) the financial harm to customers resulting from the practices; (vi) the identities of customers harmed; (vii) the amount by which each such customer was harmed; and (viii) the amount, if any, by which Gruntal was unjustly enriched as a result of such practices;
- c. review the policies and procedures that Gruntal has adopted and implemented since the activities described in this Order, to determine whether and to what extent there is a need for additional or amended policies and procedures designed reasonably to prevent and detect, insofar as practicable, violations of the federal securities laws;
- d. recommend policies and procedures (or amendments to existing policies and procedures) designed reasonably to prevent and detect, insofar as practicable, violations of the federal securities laws;
- e. be entitled, to the extent that he or she deems appropriate, to rely upon work performed or to be performed by E&Y, D&T, Gruntal's Quality Assurance Task Force, Gruntal's Operations Division, and Gruntal's Operations Control Group;
- f. be entitled, to the extent that he or she deems appropriate, to hire such persons as are reasonably necessary to perform his or her duties

as set forth in this Order, to require Gruntal to continue the engagement of D&T, and to require Gruntal to maintain resources within its Operations Control Group to support the efforts of the Independent Consultant;

- g. submit a written report to Gruntal's Board of Directors of his or her findings and recommendations, within six months of the date of this Order. Gruntal shall be provided a reasonable opportunity to comment on the Independent Consultant's review and recommendations;
- h. simultaneous with the submission of the written report referenced above to the Board of Directors of Gruntal, submit a copy of such report to the Director of the Division of Enforcement of the Commission and such other persons or entities as may be proposed by any governmental, regulatory, or self-regulatory body;
- i. conduct, on an annual basis for a period of three years commencing with the date of this Order, an audit of the policies and procedures described in Sections VI.F.2.a., c., and d. above, and the policies and procedures adopted pursuant to the Independent Consultant's recommendations, to ensure compliance with those procedures. As a result of such audit, the Independent Consultant may recommend new procedures or revisions to existing procedures, and to the system for applying such procedures, to achieve the objectives outlined in Sections VI.F.2.a., c., and d. above; and
- j. report to the Director of the Division of Enforcement of the Commission and Respondents:
 - (i) any material failure to comply with the procedures and system for applying those procedures, described in Sections VI.F.2.a., c., and d. above, and the policies and procedures adopted pursuant to the Independent Consultant's recommendations;
 - (ii) any other material failure by Respondents to comply with this Order; and
 - (iii) any violation of the federal securities laws;

3. Respondents shall adopt and implement, no later than 90 days after receipt of the Independent Consultant's report (or such other time as the Independent Consultant believes is necessary), such

policies and procedures as recommended by the Independent Consultant; provided however, that as to any of the Independent Consultant's recommendations that Gruntal determines is unduly burdensome and impractical, Gruntal may propose an alternative procedure reasonably designed to accomplish the same objectives. The Independent Consultant shall reasonably evaluate such alternative procedure and, if appropriate, either approve the alternative procedure, amend the recommendation, or reassert the original recommendation. Gruntal shall abide by the decision of the Independent Consultant and adopt and implement the alternative procedure, amended recommendation, or the original recommendation within the time period set by the Independent Consultant in light of the nature of the procedures;

4. Respondents shall pay to each customer identified by the Independent Consultant's report as having been financially harmed in connection with Gruntal's reporting or processing of OTC trades, within 90 days of the submission of the Independent Consultant's report to Gruntal's Board of Directors, an amount equal to the amount by which each such customer was harmed, plus accrued interest thereon calculated at the rate utilized by the Commission in cases involving disgorgement. If it is not possible or is impractical to make such payments to each customer harmed, then the monies not returned to customers shall be paid into the United States Treasury. In any event, Gruntal shall not retain the benefit of any monies improperly obtained in connection with the reporting or processing of OTC trades;

5. Respondents shall cooperate fully with the Fund Administrator and the Independent Consultant, including using all reasonable efforts to obtain the cooperation of Respondents' employees or other persons under their control, including E&Y and D&T, and giving the Fund Administrator and the Independent Consultant full access to all documents and premises under Respondents' control;

6. To ensure the independence of the Fund Administrator and the Independent Consultant, Respondents:

- a. shall not have the authority to terminate the Independent Consultant, or the Fund Administrator if selected by the Commission pursuant to Section VI.F.1.g. above, without the prior written

approval of the Director of the Division of Enforcement of the Commission;

- b. shall compensate the Fund Administrator, the Independent Consultant, and persons engaged to assist the Fund Administrator and Independent Consultant, for services rendered pursuant to this Order at their reasonable and customary rates;
- c. shall not, without the prior written consent of the Director of the Division of Enforcement of the Commission, enter into any legal, business, or other financial relationship with the Fund Administrator, Independent Consultant, any firm with which the foregoing are affiliated or of which they are a member, or any person engaged by the Fund Administrator or the Independent Consultant to assist the Fund Administrator or Independent Consultant in the performance of their duties under this Order, other than as described in this Order, during the period of their engagements and for a period of two years following the completion of their duties described in this Order; and
- d. shall not be in and shall not have an attorney-client relationship with the Fund Administrator or Independent Consultant and shall not seek to invoke the attorney-client or any other doctrine or privilege to prevent the Fund Administrator or Independent Consultant from transmitting any information, reports, or documents to the District Court, the Commission, or its staff;

7. If the Fund Administrator resigns or is otherwise unable to serve, a successor shall be appointed and approved by the District Court upon the Commission's recommendation and with the consent of the Respondents, which consent shall not be unreasonably withheld. Respondents shall retain such successor, at Respondents' expense, within 30 days after the successor's appointment and approval by the District Court. If the Fund Administrator is selected by the Commission pursuant to Section VI.F.1.g. above and resigns or is otherwise unable to serve, a successor shall be selected by the Commission with the consent of the Respondents, which consent shall not be unreasonably withheld. Respondents shall retain such successor, at Respondents' expense, within 30 days after the Commission's selection. If the Independent Consultant resigns or is otherwise unable to serve, Respondents shall retain a successor within 30 days, at

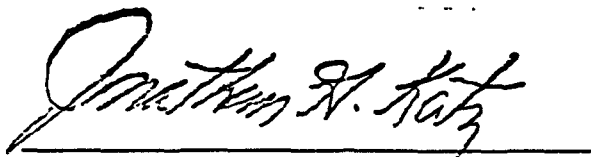
Respondents' expense, acceptable to the Commission's staff. All provisions in this Order that apply to the Fund Administrator or the Independent Consultant shall apply to any successor;

8. Gruntal shall maintain for a period of at least three years after the date of this Order a Committee of its Board of Directors (the "Committee"), consisting of no fewer than three persons, which shall: (a) review policy relating to the achievement of compliance with applicable federal securities laws and the rules and regulations of the Municipal Securities Rulemaking Board or of any national securities exchange or self-regulatory organization ("SRO") of which Gruntal is a member ("applicable rules and regulations"); (b) monitor Gruntal's implementation of any changes in Gruntal's policies and procedures adopted as a result of the Independent Consultant's review process described in Sections VI.F.2.a., c., and d. above; and (c) monitor Gruntal's efforts to detect, correct, and prevent failures to comply with applicable rules and regulations. The Committee shall require the General Counsel of Gruntal to submit quarterly to the Committee a written report which shall include a summary of: government and SRO investigations involving Gruntal or its employees; internal disciplinary actions; employee terminations for cause; and any material deficiencies in policies or procedures identified in any internal audit at Gruntal. In addition, the Committee shall provide a quarterly report to the Board of Directors of Gruntal, which shall include a summary of the activities of the Committee in ensuring the fulfillment of its responsibilities under this Order; and

9. Respondents shall cooperate, and use all reasonable efforts to cause its present or former officers, directors, agents, servants, employees, attorneys-in-fact, assigns, and all persons in active concert and participation with them to cooperate, with investigations, administrative proceedings, and litigation conducted by the Commission, other government agencies, securities exchanges, or SROs arising from or relating to the conduct described in this Order; and

G. Under no circumstances shall any of the assets referred to in Section VI. of this Order be paid to or revert to Respondents, their assigns, subsidiaries, or shareholder(s).

By the Commission.

A handwritten signature in cursive script, reading "Jonathan G. Katz". The signature is written in black ink and is positioned above a horizontal line.

Jonathan G. Katz
Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 7278 / April 9, 1996

SECURITIES EXCHANGE ACT OF 1934
Release No. 37084 / April 9, 1996

INVESTMENT ADVISERS ACT OF 1940
Release No. 1560 / April 9, 1996

ADMINISTRATIVE PROCEEDING
File No. 3-8983

In the Matter of	:	
	:	
	:	ORDER INSTITUTING
	:	PUBLIC ADMINISTRATIVE
	:	PROCEEDINGS, MAKING
GRUNTAL & CO., INCORPORATED,	:	FINDINGS, IMPOSING
	:	REMEDIAL SANCTIONS, AND
	:	ISSUING CEASE AND
	:	DESIST ORDER
Respondent.	:	
	:	

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be instituted against Gruntal & Co., Incorporated ("Gruntal") pursuant to Section 8A of the Securities Act of 1933 ("Securities Act"), Sections 15(b)(4) and 21C of the Securities Exchange Act of 1934 ("Exchange Act") and Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 ("Advisers Act"). In anticipation of the institution of these administrative proceedings, Gruntal has submitted an Offer of Settlement, which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceeding brought by or on behalf of the Commission, or to which the Commission is a party, Gruntal, by its Offer of Settlement, prior to a hearing pursuant to the Commission's Rules of Practice and without admitting or denying the findings set forth herein, consents to the entry of this Order Instituting Public Administrative Proceedings, Making Findings, Imposing Remedial Sanctions, and Issuing Cease and Desist Order ("Order").

II.

Accordingly, IT IS HEREBY ORDERED that proceedings pursuant to Section 8A of the Securities Act, Sections 15(b)(4) and 21C of the Exchange Act, and Sections 203(e) and 203(k) of the Advisers Act be, and hereby are, instituted.

III.

The Commission makes the following findings:^{1/}

Respondent

A. At all times from January 1, 1993 to the present, Gruntal has been a broker-dealer registered with the Commission pursuant to Section 15(b) of the Exchange Act and has been an investment adviser registered with the Commission pursuant to Section 203(c) of the Advisers Act. Throughout that period, Gruntal has been a member of several national securities exchanges, including the New York Stock Exchange, Inc. ("NYSE"), and of the National Association of Securities Dealers, Inc. As a broker-dealer, Gruntal provides a full range of securities brokerage and trading services, as well as related financial services. As an investment adviser, Gruntal manages client accounts or advises on the selection and monitoring of other investment managers. According to Gruntal's Form ADV filed on September 29, 1994, Gruntal advised 325 clients with assets of \$164 million.

Summary

B. This proceeding involves violations of the antifraud and record-keeping provisions of the federal securities laws in connection with Gruntal's execution of brokerage transactions for investment advisory clients and other customers. Between January 1993 and November 1995, Gruntal, through its three investment advisory divisions, executed at least 8,813 transactions for its advisory clients on a principal basis or by crossing advisory client orders with orders for other Gruntal customers. These transactions were contrary to the disclosure in Gruntal's Form ADV and in many instances violated the notice and consent requirements of the Advisers Act. In addition, confirmations sent to advisory clients and other Gruntal brokerage clients wrongly identified certain principal transactions as agency transactions. Gruntal also charged commissions, commission equivalents or mark-ups/mark-downs (collectively, "transaction charges") on transactions for certain advisory clients who had

^{1/} The findings herein and the entry of this Order are solely for the purposes of this proceeding and shall not be binding on any other person or entity named in any other proceeding.

chosen to pay only an asset-based fee to Gruntal for brokerage and execution services ("fee-only clients"), contrary to statements in Gruntal's Form ADV and brochures provided to clients. From March 1995 to November 1995, Gruntal also failed to disclose to its advisory clients that it received payment for directing order flow to two affiliated broker-dealers. Finally, Gruntal failed to keep and maintain accurate records concerning the capacity in which it executed transactions.

Gruntal's Investment Advisory Divisions

C. At all times from January 1993 to the present, Gruntal has provided investment advisory services through three divisions: Managed Accounts, Sterling Advisors and Professional Asset Management ("PAM").

D. Managed Accounts and Sterling provide investment advisory services on both a discretionary and non-discretionary basis. Clients are offered a choice of fee arrangements including (1) an all-inclusive fee based on a percentage of total assets under management or (2) a management fee based on a percentage of total assets under management and a separate payment for custody and execution services.

E. PAM provides various services including establishing investment guidelines and objectives, selecting appropriate investment managers and monitoring investment performance. PAM does not have any discretionary authority over its clients' accounts but rather recommends non-affiliated investment advisers. PAM's clients pay their investment advisers separately. PAM's clients may direct that all transactions for their accounts be executed through Gruntal and have two alternatives for compensating Gruntal: (1) an all-inclusive fee based on a percentage of total assets under management; or (2) Gruntal's standard commission schedule.

F. At all relevant times, Gruntal's Form ADV has stated that the all-inclusive fee for Sterling includes "advisory services, trade execution and settlement, custodial fees, and accounting services. . . ." Gruntal distributed brochures to Sterling and Managed Accounts clients which state that the all-inclusive fee for Managed Accounts and Sterling covers "both investment advisory services and custody (Gruntal only) and execution services with no separate charged [sic] imposed for brokerage commissions on agency trades or markups or markdowns on principal transactions, except mutual fund purchases and syndicate issues, if any."

G. At all relevant times, Gruntal's Form ADV has stated with respect to PAM that "the client may pay a pre-determined, asset based commission that covers all trading related charges for the account (with the exception of certain minor NYSE

charges) no matter what the trading activity." Gruntal distributed brochures to PAM clients which state that PAM's asset-based commission covers "PAM consulting services and all custody (Gruntal only) and execution services with no separate charge imposed for brokerage commissions on agency trades or markups or markdowns on principal transactions, except mutual fund purchases and syndicate issues, if any."

H. On September 27, 1994, Gruntal filed the Sterling, Managed Accounts, and PAM brochures with the Commission, as Schedule H to Gruntal's Form ADV.

The 1992 Examination and Related Representations by Gruntal

I. An examination of Gruntal's investment advisory activities conducted by the Commission's staff in late 1992 revealed various deficiencies. As the staff advised Gruntal in a deficiency letter dated January 29, 1993, among other things: (1) Gruntal had failed to comply with the notice and consent requirements of Section 206(3) of the Advisers Act with respect to principal and agency cross transactions; (2) Gruntal's Form ADV, which stated that Gruntal generally did not effect principal transactions with its advisory clients and would, in substance, comply with the notice and consent requirements of the Advisers Act in the event that Gruntal did effect such transactions, was inaccurate in that Gruntal had in fact executed transactions on a principal basis with its advisory clients without complying with such requirements; (3) Gruntal's Form ADV failed to disclose that Gruntal effected agency cross transactions with its advisory clients; and (4) Gruntal had improperly imposed transaction charges on certain trades for its fee-only clients' accounts.

J. In response to the staff's deficiency letter, Gruntal informed the staff in writing that Gruntal was amending its Form ADV and that it was creating a special order ticket to be used when effecting transactions for advisory clients' accounts. The special order ticket was to carry a notice stating: "Agency Transaction - Do not Cross" to prevent principal and agency cross transactions from being effected.

K. Gruntal filed an amended Form ADV on March 30, 1993 which stated, in pertinent part:

Gruntal & Co. does not permit principal or cross transactions with investment advisory clients. A special order ticket is utilized for advisory clients which states "Agency Transaction - Do not Cross" to ensure compliance with the above. In addition, managers of those areas review all transactions daily to ensure that orders are entered and executed properly.

The Principal and Agency Cross Transactions

L. From January 1993 through November 1995 (the "relevant period"), Gruntal executed at least 8,792 purchases and sales of securities for advisory clients on a principal basis and at least 21 transactions on an agency cross basis. Gruntal did not disclose to the clients (including clients of Managed Accounts and Sterling whose accounts were managed by Gruntal) in writing, prior to the completion of each such transaction, the capacity in which Gruntal was acting in the transaction and did not obtain client consent thereto.

M. On certain of the principal trades, as well as for certain principal trades involving non-advisory brokerage customers, Gruntal wrongly stated in customer confirmations that it had acted as agent in the transaction when, in fact, Gruntal had acted as principal.

N. Contrary to its representations to the staff and in its Form ADV, Gruntal never used the new order tickets when effecting transactions for its advisory clients' accounts and did not adequately review all transactions daily to ensure that orders for advisory clients' accounts were executed properly.

O. In certain of the principal transactions, clients were disadvantaged in that Gruntal caused them to pay transaction charges greater than the amount of commission the client (other than a fee-only advisory client) would have been charged had the transaction been executed on an agency basis.

P. Certain of the transactions referred to above were executed other than on a national securities exchange.

The Transaction Charges on Certain Trades For Fee-Only Clients

Q. During the relevant period, Gruntal imposed transaction charges on certain trades for advisory clients who had chosen to pay Gruntal an all-inclusive, asset-based fee. In many of these transactions, Gruntal did not disclose such transaction charges in customer confirmations. Imposing the transaction charges was contrary to the representations in Gruntal's Form ADV and the brochures provided to clients.

Payment for Order Flow

R. From March 1995 through November 1995, Gruntal effected additional purchases and sales of securities for advisory clients through two registered broker-dealers which are 99.9% owned by a limited liability company in which Gruntal owns an interest exceeding ten percent. Gruntal received payment for directing trades to these broker-dealers.

S. Item 13 of Part II of Form ADV requires an adviser to describe additional compensation it receives from non-clients in connection with giving advice to clients. Gruntal did not disclose Gruntal's financial interest in the affiliated broker-dealers, or Gruntal's receipt of payments for order flow in its Form ADV.

Failure to Maintain Accurate Books and Records

T. Gruntal's customer confirmations and other records in some instances wrongly stated that brokerage transactions had been executed on an agency basis when they were in fact executed on a principal basis. Gruntal therefore failed to maintain an accurate memorandum of certain customer orders, for both advisory clients and non-advisory customers, showing the terms and conditions of such orders. Specifically, Gruntal failed to maintain an accurate memorandum showing the capacity in which Gruntal acted in certain transactions.

IV.

Violations

A. Section 17(a) of the Securities Act prohibits, in the offer or sale of securities, (1) devices, schemes, or artifices to defraud, (2) misrepresentations or omissions of material facts, or (3) transactions, practices, or courses of business that would operate as a fraud. Section 10(b) of the Exchange Act and Rule 10b-5 thereunder prohibit devices, schemes, and artifices to defraud in connection with the purchase or sale of securities. Sections 206(1) and 206(2) of the Advisers Act prohibit an investment adviser from employing any device, scheme, or artifice to defraud clients or engage in any transaction, practice, or course of business that defrauds clients. *Scienter* is a required element to prove violations of Section 17(a)(1), Section 10(b) and Rule 10b-5, and Section 206(1). Aaron v. SEC, 446 U.S. 680, 701-02 (1980); Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976); Steadman v. SEC, 603 F.2d 1126, 1134 (5th Cir. 1979), aff'd on other grounds, 450 U.S. 91 (1981).

B. Gruntal violated Section 17(a), Section 10(b) and Rule 10b-5, and Sections 206(1) and 206(2) by (1) falsely representing to advisory clients in its Form ADV that it did not execute principal or agency cross transactions for its advisory clients, (2) falsely representing to fee-only advisory clients that it did not impose transaction charges on trades it executed for them; and (3) failing to disclose to advisory clients that it received payment for directing trades to two affiliated broker-dealers.

C. Section 206(3) of the Advisers Act prohibits an investment adviser from effecting transactions for its advisory clients on a principal or agency cross basis without, in each instance, notifying the clients in writing, prior to the completion of the transaction, of the capacity in which the investment adviser is acting and obtaining the client's consent.

D. Gruntal violated Section 206(3) by executing transactions for clients of Managed Accounts and Sterling on a principal or agency cross basis without, prior to the completion of the transaction, disclosing the capacity in which it acted in the transaction and without obtaining the client's consent thereto.

E. Section 15(c) of the Exchange Act, and Rules 10b-3(a) and 15c1-2 thereunder prohibit any broker or dealer from employing any manipulative, deceptive, or otherwise fraudulent device or contrivance when effecting any transaction in any security otherwise than on a national securities exchange. Rule 10b-10(a)(2) (prior to April 3, 1995, Rule 10b-10(a)(1)), requires brokers to provide their customers with written notification at or before completion of each transaction specifying the capacity in which the broker is acting when executing the transaction.

F. Gruntal violated Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act, Rules 10b-3(a), 10b-5, 10b-10(a)(2) and 15c1-2 under the Exchange Act, and Sections 206(1) and 206(2) of the Advisers Act by falsely identifying transactions on advisory client and other customer confirmations as agency transactions when such transactions were in fact principal transactions.

G. Section 207 of the Advisers Act prohibits the willful making of untrue statements of material fact in applications and reports required to be filed with the Commission pursuant to Section 203 and 204 of the Advisers Act or the omission in such applications and reports of material facts required to be stated therein.

H. Gruntal violated Section 207 by (1) willfully making the following false statements in its Form ADV: (a) that Gruntal did not permit principal and agency cross transactions with advisory clients, (b) that Gruntal utilized certain specified procedures to prevent and detect such transactions, and (c) that clients choosing to pay an asset-based fee would not pay separate transaction charges and by (2) willfully omitting to disclose: (a) the arrangement by which Gruntal received payment for directing order flow to certain broker-dealers, and (b) that Gruntal executed certain transactions through other broker-dealers in which it has an ownership interest and for which it clears transactions.

I. Section 17(a) of the Exchange Act and Rule 17a-3 thereunder require registered broker-dealers to make and keep certain books and records. The requirement that certain books and records be made also requires that those records be made accurately. U.S. v. Sloan, 389 F. Supp. 526, 528 (S.D.N.Y. 1975); In the Matter of Michael Alan Pettis, Exchange Act Release No. 33254 (Nov. 29, 1993). The Commission has emphasized the importance of the records maintained by broker-dealers pursuant to the Exchange Act, describing them as the "keystone of the surveillance of brokers and dealers by our staff and by the securities industry's self-regulatory bodies." Edward J. Mawod & Co., 46 SEC 865, 873 n.39 (1977), aff'd, 591 F.2d 588 (10th Cir. 1979). Rule 17a-3(a)(6) requires a broker-dealer to maintain a memorandum of each brokerage order or other instruction given or received for the purchase or sale of securities, showing the terms and conditions of the order or instructions.

J. Gruntal violated Section 17(a) and Rule 17a-3 by failing to maintain an accurate memorandum of each brokerage order correctly reflecting the capacity in which the order was executed by Gruntal.

K. Section 204 of the Advisers Act and Rule 204-2 require registered investment advisers to make and keep certain books and records. Rule 204-2(a)(3) requires an investment adviser to maintain, among other things, a memorandum of each order given by the adviser for the purchase or sale of a security, showing the terms and conditions of the order.

L. Gruntal violated Section 204(a) and Rule 204-2 by failing to maintain an accurate memorandum of each brokerage order correctly reflecting the capacity in which the order was executed by Gruntal.

M. While engaged in the conduct described above, Gruntal, directly and indirectly, used the means or instrumentalities of interstate commerce or the mails.

V.

Based on the foregoing, the Commission finds that Gruntal willfully violated Section 17(a) of the Securities Act, Sections 10(b), 15(c) and 17(a) of the Exchange Act and Rules 10b-3, 10b-5, 10b-10, 15c1-2 and 17a-3(a)(6) thereunder, and Sections 204, 206(1), (2), and (3) and 207 of the Advisers Act and Rule 204-2 thereunder.

VI.

In view of the foregoing, it is in the public interest to impose the sanctions specified in the Offer of Settlement.

Accordingly, IT IS HEREBY ORDERED that:

- A. Gruntal be, and hereby is, censured;
- B. Gruntal, pursuant to Section 8A of the Securities Act, Section 21C of the Exchange Act, and Section 203(k) of the Advisers Act, cease and desist from committing or causing any violation, and any future violation, of Section 17(a) of the Securities Act, Sections 10(b), 15(c) and 17(a) of the Exchange Act and Rules 10b-3, 10b-5, 10b-10, 15c1-2 and 17a-3(a)(6) thereunder, and Sections 204, 206(1), (2), and (3) and 207 of the Advisers Act and Rule 204-2 thereunder;
- C. Gruntal shall pay a civil money penalty in the amount of \$1 million pursuant to Section 21B of the Exchange Act and Section 203(i) of the Advisers Act. Such payment shall be: (1) made by United States postal money order, certified check, bank cashier's check, or bank money order; (2) made payable to the Securities and Exchange Commission; (3) hand-delivered, within 10 business days of the date of this Order, to the Comptroller, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549; and (4) submitted under cover letter identifying Gruntal as a Respondent in these proceedings, and the Commission's case number (NY-6306), a copy of which shall be sent to Wayne M. Carlin, Assistant Regional Director, Northeast Regional Office, U.S. Securities and Exchange Commission, 7 World Trade Center, 13th floor, New York, N.Y. 10048;
- D. Gruntal shall comply with the following undertakings:
 1. Gruntal shall retain, within 45 days of the date of this Order, at Gruntal's expense, an Independent Consultant, acceptable to the staff of the Northeast Regional Office of the Commission, to:
 - a. conduct a comprehensive review of Gruntal's policies and procedures concerning: (i) execution of orders for advisory client accounts managed by Gruntal and for Gruntal fee-only clients, including but not limited to principal and agency-cross transactions and execution by broker-dealers from whom Gruntal receives payments for order flow; and (ii) the coding, and reporting on client confirmations and internal Gruntal records, of brokerage transactions executed by Gruntal with respect to the capacity in which such transactions are executed;

- b. review any policies and procedures that Gruntal has adopted and implemented since the activities described in this Order, to determine whether and to what extent there is a need for additional or amended policies and procedures designed reasonably to prevent and detect, insofar as practicable, the same or similar violations of the federal securities laws;
- c. recommend policies and procedures (or amendments to existing policies and procedures) designed reasonably to prevent and detect, insofar as practicable, the same or similar violations of the federal securities laws;
- d. (i) identify all advisory clients and brokerage customers financially harmed by the improper principal and agency cross transactions, improper transaction charges on trades for fee-only clients, and principal transactions improperly identified as agency transactions on client confirmations, and (ii) quantify the amount of financial harm to each such client;
- e. quantify the amount of payment Gruntal received for order flow on transactions executed for advisory client accounts;
- f. be entitled, to the extent that he or she deems appropriate, to rely upon work performed or to be performed by Ernst & Young LLP ("E&Y"), Deloitte & Touche LLP ("D&T"), Gruntal's Quality Assurance Task Force, and Gruntal's Operations Department, including but not limited to, Gruntal's Operations Control Group;
- g. be entitled, to the extent that he or she deems appropriate, to hire such persons as are reasonably necessary to perform his or her duties as set forth in this Order, to require Gruntal to continue the engagement of D&T, and to require Gruntal to maintain resources within its Operations Control Group to support the efforts of the Independent Consultant;
- h. submit a written report to Gruntal's Board of Directors of his or her findings and recommendations, within six months of the date of this Order. Gruntal shall be provided a reasonable opportunity, but in no event less than

30 days, to comment on the Independent Consultant's review and recommendations;

- i. simultaneous with the submission of the written report referenced above to the Board of Directors of Gruntal, submit a copy of such report to the staff of the Northeast Regional Office of the Commission;
- j. conduct, on an annual basis for a period of three years commencing with the date of this Order, an audit of the policies and procedures described in Paragraphs VI.D.1.a. through c. above, and the policies and procedures adopted pursuant to the Independent Consultant's recommendations, to ensure compliance with those procedures. As a result of such audit, the Independent Consultant may recommend new procedures or revisions to existing procedures, and to the system for applying such procedures, to achieve the objectives outlined in Paragraph VI.D.1.a. through c. above; and
- k. report to the staff of the Northeast Regional Office of the Commission and Gruntal: (i) any material failure to comply with the procedures and system for applying those procedures, described in Paragraphs VI.D.1.a. through c. above, and the policies and procedures adopted pursuant to the Independent Consultant's recommendations; and (ii) any other material failure by Gruntal to comply with this Order;

2. Gruntal shall adopt and implement, no later than 90 days after receipt of the Independent Consultant's report (or such other time as the Independent Consultant believes is necessary), such policies and procedures as recommended by the Independent Consultant; provided however, that as to any of the Independent Consultant's recommendations that Gruntal determines is unduly burdensome and impractical, Gruntal may propose an alternative procedure reasonably designed to accomplish the same objectives. The Independent Consultant shall reasonably evaluate such alternative procedure and, if appropriate, either approve the alternative procedure, amend the recommendation, or reassert the original recommendation. Gruntal shall abide by the decision of the Independent Consultant and adopt and implement the alternative procedure, amended recommendation, or the original recommendation within the time period set by

the Independent Consultant in light of the nature of
the procedures;

3. Gruntal shall pay to each client identified by the Independent Consultant's report as having been financially harmed pursuant to Paragraph VI.D.1.d. above, within 90 days of the submission of the Independent Consultant's report to Gruntal's Board of Directors, an amount equal to the amount by which each such client was harmed plus accrued interest thereon, calculated at the Internal Revenue Service rate of interest on tax underpayments, compounded quarterly, excluding partial months, from the date of the violation to the date of this Order. If it is not possible or is impractical to make such payments to each client harmed, then the monies not returned to customers shall be paid into the United States Treasury. In any event, Gruntal shall not retain the benefit of any monies improperly obtained in connection with the violations referred to herein;

4. Gruntal shall pay into the United States Treasury the amount of payment Gruntal received for order flow on transactions executed for advisory client accounts determined by the Independent Consultant's report plus accrued interest thereon, calculated at the Internal Revenue Service rate of interest on tax underpayments, compounded quarterly, excluding partial months, from the date of the violation to the date of this Order, within 45 days of the submission of the Independent Consultant's report to Gruntal's Board of Directors;

5. Gruntal shall cooperate fully with the Independent Consultant, including using all reasonable efforts to obtain the cooperation of Gruntal's employees or other persons under their control, including E&Y and D&T, and giving the Independent Consultant full access to all documents and premises under Gruntal's control;

6. To ensure the independence of the Independent Consultant, Gruntal:

- a. shall not have the authority to terminate the Independent Consultant, without the prior written approval of the staff of the Northeast Regional Office of the Commission;
- b. shall compensate the Independent Consultant, and persons engaged to assist the Independent Consultant for services rendered pursuant to this Order at their reasonable and customary rates;

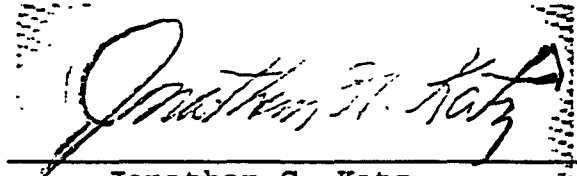
- c. shall not, without the prior written consent of the staff of the Northeast Regional Office of the Commission, enter into any legal, business, or other financial relationship with the Independent Consultant, any firm with which he or she is affiliated or of which he or she is a member, or any person engaged to assist the Independent Consultant in the performance of his or her duties under this Order, other than as described in this Order, during the period of their engagements and for a period of two years following the completion of their duties described in this Order; and
- d. shall not be in and shall not have an attorney-client relationship with the Independent Consultant and shall not seek to invoke the attorney-client or any other doctrine or privilege to prevent the Independent Consultant from transmitting any information, reports, or documents to the Commission or its staff;

7. Gruntal shall maintain for a period of at least three years after the date of this Order a Committee of its Board of Directors (the "Committee"), consisting of no fewer than three persons, which shall: (a) monitor Gruntal's implementation of any changes in Gruntal's policies and procedures adopted as a result of the Independent Consultant's review process described in Paragraphs VI.D.1.a. through c. above; and (b) monitor Gruntal's efforts to detect, correct, and prevent failures to comply with applicable rules and regulations. The Committee shall provide a quarterly report to the Board of Directors of Gruntal, which shall include a summary of the activities of the Committee in ensuring the fulfillment of its responsibilities under this Order; and

8. Gruntal shall cooperate, and use all reasonable efforts to cause its present or former officers, directors, agents, servants, employees, attorneys-in-fact, assigns, and all persons in active concert and participation with them to cooperate, with investigations, administrative proceedings, and litigation conducted by the Commission, other

government agencies, securities exchanges, or SROs arising from or relating to the conduct described in this Order.

By the Commission.

A handwritten signature in cursive script, appearing to read "Jonathan G. Katz", is written over a horizontal line. The signature is enclosed within a rectangular border that has a dotted or perforated appearance on its left and right sides.

Jonathan G. Katz
Secretary

the public certain materially false and misleading annual and quarterly reports and a materially false and misleading registration statement that overstated Gruntal Financial's income and failed to disclose the involvement of certain members of senior management in the diversions.

3. In 1987, Gruntal Financial was acquired by The Home Group, Inc. In connection with that acquisition, and while in possession of material non-public information about the fraudulent scheme described in this complaint, Bao contracted with the Home Group to sell a total of 618,000 shares of Gruntal Financial common stock, thereby avoiding substantial losses. He also falsely represented that Gruntal Financial's SEC filings contained no material misstatements and that Gruntal was conducting its business in compliance with applicable laws.

4. As described more fully below, Bao violated the federal securities laws by engaging in the fraudulent diversion scheme and by selling Gruntal Financial securities without disclosing the scheme, and unless enjoined is likely to commit such violations in the future.

JURISDICTION

5. This Court has jurisdiction over this action pursuant to Sections 20(b) and 22(a) of the Securities Act of 1933 [15 U.S.C. §§ 77t(b) and 77v(a)] and Sections 21(d), 21(e), and 27 of the Securities Exchange Act of 1934 [15 U.S.C. §§ 78u(d), 78u(e), and 78aa].

6. Bao, directly or indirectly, used the means and instrumentalities of interstate commerce, of the mails, or of the facilities of a national securities exchange in connection with the transactions, acts, practices, and courses of business alleged herein.

THE DEFENDANT

7. From December 1983 to December 1994, Bao was a director and Executive Vice President for Operations and Administration of both Gruntal and Gruntal Financial. He is no longer employed by Gruntal or Gruntal Financial.

THE ISSUER

8. At all times relevant, Gruntal Financial was a Delaware corporation with its principal place of business in New York City engaged in the operation of a full-service brokerage business through its wholly-owned subsidiary, Gruntal. Until it was acquired by the Home Group in August 1987, Gruntal Financial's securities were registered with the Commission pursuant to Section 12(b) of the Exchange Act [15 U.S.C. § 78l(b)] and traded on the New York Stock Exchange.

9. At all times relevant, Gruntal has been a broker-dealer registered with the Commission pursuant to Section 15(b) of the Exchange Act [15 U.S.C. § 78o(b)].

FACTS

THE FRAUDULENT DIVERSION SCHEME

Diverting Checks, Dividends, and Other Assets

10. Beginning in at least 1984, Bao directed certain managers and employees at Gruntal to divert stale customer and vendor checks, balances and securities from dormant customer accounts, and unclaimed dividends for the purpose of inflating Gruntal's income and reducing its expenses. As part of the scheme, Bao established, or directed the establishment of, fictitious customer accounts at Gruntal and directed that the diverted assets be transferred to the fictitious accounts. Bao was assisted in the diversions by Gruntal's Director of Operations, its Manager of Internal Audit, and its Executive Cashier, each of whom acted at Bao's direction.

11. At Bao's direction, diverted assets totaling approximately \$5 million were transferred out of the fictitious customer accounts and into Gruntal profit and loss accounts or used to fund off-books cash payments of certain Gruntal expenses.

Altering and Falsifying Books and Records

12. At Bao's direction, various Gruntal books and records were altered or falsified to conceal the diversions. In furtherance of the diversion scheme, Bao, or others acting at his direction, created false dividend claim forms, debit and credit advices, debit and credit memos, and bookkeeping journal entries. Bao and those acting at his direction created these false records to conceal the fraudulent nature of the transactions.

13. Bao, or others acting at his direction, also opened accounts in the names of fictitious companies and created false account opening documents, account statements, and account statement entries.

14. As a consequence of Bao's diverting assets in this fashion to Gruntal profit and loss accounts or using them to make off-books payments of Gruntal expenses, Gruntal overstated its revenues, understated its expenses, and, consequently, overstated its income.

15. Because Gruntal Financial is a holding company that conducts its business through Gruntal, Bao's falsifying Gruntal's books, records, and accounts also resulted in falsification of Gruntal Financial's books, records, and accounts. And because Bao succeeded in inflating Gruntal's income, he also thereby inflated Gruntal Financial's income.

THE FALSE FILINGS

16. From 1985 through the third quarter of fiscal 1987, as a result of Bao's scheme, Gruntal Financial filed with the Commission certain false and misleading periodic reports and a false and misleading registration statement. These filings, including the financial statements contained therein, were materially misstated because they failed to reflect or disclose the amounts and uses of the diverted assets. As a result, the filings overstated Gruntal Financial's income.

17. In June 1986, Gruntal Financial filed a registration statement on Form S-1 (and Amendment No. 1 thereto) with the

Commission to register a public offering of convertible subordinated debentures and the underlying common stock. The financial statements included in those filings overstated Gruntal Financial's fiscal 1985 pre-tax income by 15 percent. The financial statements included in Gruntal Financial's Form 10-K for fiscal 1985 likewise overstated pre-tax income by 15 percent. The financial statements in Gruntal Financial's Form 10-Q for the third quarter of fiscal 1987 overstated pre-tax income by 8 percent. In each instance, the overstatement of income was materially false and misleading. Moreover, none of the reports disclosed the involvement of certain members of senior management in the diversion of assets.

BAO'S ILLEGAL TRADING

18. On June 24, 1987, while Bao was a director of Gruntal Financial, the Board of Directors of Gruntal Financial unanimously approved resolutions approving a merger agreement with the Home Group pursuant to which Gruntal Financial and an acquisition subsidiary of the Home Group would be merged and each share of outstanding Gruntal Financial common stock would be converted into the right to receive \$9.50 in cash.

19. As part of the merger agreement, Gruntal Financial represented and warranted that none of the reports, schedules, registration statements, or definitive proxy statements filed by Gruntal Financial with the Commission since January 1, 1986, "contained any untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary

in order to make the statements therein, in light of the circumstances under which they were made, not misleading," that those filings "complied in all material respects with the requirements" of the Securities Act, the Exchange Act, and the Commission's rules and regulations thereunder, and that the financial statements included in those filings had "been prepared in accordance with generally accepted accounting principles." Gruntal Financial further represented and warranted that, except as had been disclosed, the businesses of Gruntal Financial and its subsidiaries "are not being conducted in violation of any law, ordinance or regulation of any Governmental Entity."

20. On June 24, 1987, Bao and certain other Gruntal Financial insiders entered into a stock purchase agreement with the Home Group pursuant to which Bao sold a total of 618,000 shares of Gruntal Financial common stock (582,000 shares for his own account and another 36,000 shares as trustee for certain trusts). All 618,000 shares were sold at \$9.50 per share, resulting in total proceeds of \$5,871,000.

21. As part of the stock purchase agreement, Bao represented and warranted that the representations and warranties of Gruntal Financial set forth in the merger agreement were true and correct.

FIRST CLAIM

Violations of Section 17(a) of the Securities Act,
Section 10(b) of the Exchange Act,
and Rule 10b-5 thereunder
in connection with the fraudulent diversion scheme

22. The Commission realleges and incorporates by reference Paragraphs 1 through 17 above.

23. At Bao's direction, and in furtherance of the fraudulent diversion scheme, certain Gruntal managers removed balances and securities from customers' securities accounts, purchased securities with the stolen balances, sold customers' securities, took customer checks representing proceeds of securities transactions, and misappropriated dividends payable to contra-brokers, institutional investors, and Gruntal's customers.

24. By reason of the foregoing, Bao violated Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)], Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)], and Rule 10b-5 [17 C.F.R. § 240.10b-5] promulgated thereunder.

SECOND CLAIM

Violations of Section 17(a) of the Securities Act,
Section 10(b) of the Exchange Act,
and Rule 10b-5 thereunder in connection with
false and misleading filings with the Commission

25. The Commission realleges and incorporates by reference Paragraphs 1 through 21 above.

26. Bao was responsible for Gruntal Financial filing with the Commission, from 1985 to mid-1987, a Form S-1 registration statement and amendment thereto and certain annual and quarterly

reports that contained materially false and misleading financial statements and omitted disclosure of the diversions.

27. Bao, as a director, signed Gruntal Financial's Form S-1 registration statement and amendment thereto and its annual reports on Form 10-K for fiscal 1985 and 1986 when he knew, or was reckless in not knowing, that they contained materially false and misleading financial statements and omitted disclosure of the diversions.

28. By reason of the foregoing, Bao violated Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act, and Rule 10b-5 thereunder.

THIRD CLAIM

Violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act, and Rule 10b-5 thereunder in connection with Bao's sale of stock while in possession of material non-public information

29. The Commission realleges and incorporates by reference Paragraphs 1 through 21 and 26 through 27 above.

30. Bao sold 618,000 shares of Gruntal Financial common stock while in possession of material non-public information. He did not disclose that information prior to selling his shares; in fact, he made specific representations and warranties that were directly contrary to what he knew.

31. By selling Gruntal Financial common stock pursuant to specific misrepresentations and without disclosing material non-public information in his possession, Bao avoided substantial losses.

32. By reason of the foregoing, Bao violated Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act, and Rule 10b-5 thereunder.

FOURTH CLAIM

**Violations of Section 13(b)(5) of the Exchange Act
and Rule 13b2-1 thereunder in connection with
falsified books and records and intentional
circumvention of internal controls**

33. The Commission realleges and incorporates by reference Paragraphs 1 through 17 above.

34. By falsifying the books and records of Gruntal, Bao knowingly falsified, or caused to be falsified, the books and records of Gruntal Financial, ensuring that those books and records did not fairly and accurately reflect the transactions or dispositions of the assets of Gruntal Financial. He also knowingly circumvented Gruntal Financial's internal controls.

35. By reason of the foregoing acts and practices, Bao violated Section 13(b)(5) of the Exchange Act [15 U.S.C. § 78m(b)(5)] and Rule 13b2-1 [17 C.F.R. § 240.13b2-1] promulgated thereunder.

FIFTH CLAIM

**Violations of Rule 13b2-2
under the Exchange Act in connection
with misstatements and omissions to
Gruntal Financial's independent auditors**

36. The Commission realleges and incorporates by reference Paragraphs 1 through 17 above.

37. From 1985 through July 1987, Bao, or certain managers and employees acting at Bao's direction, provided or made

available to the independent auditors, in connection with their audits of Gruntal Financial's financial statements, falsified documents and records, including bookkeeping journals, debit and credit memos, and other falsified records and documents, as more fully described above.

38. By creating, and directing the creation of, false or fictitious books, records, and accounts, Bao caused false and misleading statements and documents to be given to the independent auditors of Gruntal Financial. Bao failed to disclose the diversions to the independent auditors.

39. By reason of the foregoing, Bao violated Rule 13b2-2 [17 C.F.R. § 240.13b2-2] promulgated under the Exchange Act.

PRAYER

WHEREFORE, the Commission respectfully requests that this Court:

I.

Permanently enjoin Bao from violating Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)], Sections 10(b) and 13(b)(5) of the Exchange Act [15 U.S.C. §§ 78j(b) and 78m(b)(5)], and Exchange Act Rules 10b-5, 13b2-1, and 13b2-2 [17 C.F.R. §§ 240.10b-5, 240.13b2-1, and 240.13b2-2].

II.

Enter an Order, pursuant to Section 20(e) of the Securities Act [15 U.S.C. § 77t(e)] and Section 21(d)(2) of the Exchange Act [15 U.S.C. § 78u(d)(2)], permanently barring Bao from acting as an officer or director of any issuer that has a class of

securities registered pursuant to Section 12 of the Exchange Act [15 U.S.C. § 78l] or that is required to file reports pursuant to Section 15(d) of the Exchange Act [15 U.S.C. § 78o(d)].

III.

Order Bao to disgorge all illegal profits and losses avoided as a result of his 1987 sale of Gruntal Financial common stock, together with prejudgment interest thereon; and

IV.

Grant such other relief as this Court may deem just and appropriate.

Respectfully submitted,

Dated: April 9, 1976

Thomas C. Newkirk

Thomas C. Newkirk (TN 7271)
Leo F. Orenstein
James T. Coffman
Antonia Chion
Jahan P. Raissi
David Frohlich

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UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION,	:	96 Civ.
	:	
Petitioner,	:	
	:	
v.	:	PETITION FOR AN ORDER
	:	PURSUANT TO SECTION 20(c)
GRUNTAL & CO., INCORPORATED	:	OF THE SECURITIES ACT
	:	OF 1933 AND SECTION
and GRUNTAL FINANCIAL CORP.,	:	21(e) OF THE SECURITIES
	:	EXCHANGE ACT OF 1934
	:	
Respondents.	:	

Petitioner Securities and Exchange Commission ("Commission") alleges in support of its Petition as follows:

1. On April 9, 1996, the Commission issued an Administrative Order against Gruntal & Co., Incorporated ("Gruntal") under Section 8A of the Securities Act of 1933 ("Securities Act") and Sections 15(b)(4) and 21C of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. §§ 77h-1, 78o(b)(4), and 78u-3] and against Gruntal Financial Corp. ("Gruntal Financial") under Section 8A of the Securities Act and Section 21C of the Exchange Act [15 U.S.C. §§ 77h-1 and 78u-3]. In the Matter of Gruntal & Co., Incorporated and Gruntal Financial Corp., Administrative Proceeding File No. (April 9, 1996) (the "Administrative Order") (attached as Exhibit A). Gruntal and Gruntal Financial each consented to the issuance of the Administrative Order, without admitting or denying the findings therein, and to the imposition of certain remedial sanctions.

Jurisdiction and Venue

2. The Commission brings this action pursuant to Section 20(c) of the Securities Act and Section 21(e) of the Exchange Act [15 U.S.C. §§ 77t(c) and 78u(e)], for an Order of this Court requiring Gruntal and Gruntal Financial each to comply with the Commission's Administrative Order, and for other equitable relief.

3. Gruntal and Gruntal Financial maintain their principal offices in New York, New York and conduct business in the Southern District of New York on a regular basis.

4. This Court has jurisdiction over this action pursuant to Sections 20(c) and 22(a) of the Securities Act [15 U.S.C. §§ 77t(c) and 77v(a)] and Sections 21(e) and 27 of the Exchange Act [15 U.S.C. §§ 78u(e) and 78aa].

Respondents

5. Gruntal is a broker-dealer registered with the Commission pursuant to Section 15(b) of the Exchange Act [15 U.S.C. § 78o(b)]. Gruntal is a member of several national securities exchanges, including the New York Stock Exchange, Inc., and of the National Association of Securities Dealers, Inc. As a broker-dealer, Gruntal provides a full range of securities brokerage and trading services, as well as related financial services.

6. Gruntal Financial is a Delaware corporation operating a securities brokerage business through Gruntal, its wholly owned subsidiary.

Facts

7. The Commission issued the Administrative Order on April 9, 1996, against Gruntal pursuant to Section 8A of the Securities Act and Sections 15(b)(4) and 21C of the Exchange Act [15 U.S.C. §§ 77h-1, 78o(b)(4), and 78u-3] and against Gruntal Financial pursuant to Section 8A of the Securities Act and Section 21C of the Exchange Act [15 U.S.C. §§ 77h-1 and 78u-3]. In the Administrative Order, the Commission found that, among other things, Gruntal and Gruntal Financial violated the antifraud, reporting, and record-keeping provisions of the federal securities laws in connection with three separate schemes occurring between 1984 and 1994 that diverted securities and funds totaling over \$11 million from customer accounts and other sources at Gruntal. Approximately \$5 million of the diverted assets were used artificially to inflate Gruntal's income or reduce its expenses. Gruntal and Gruntal Financial each consented to the issuance of the Administrative Order prior to a hearing pursuant to the Commission's Rules of Practice, 17 C.F.R. § 201.100 et seq., without admitting or denying the findings therein, and to the imposition of certain remedial sanctions.

Petition for Order

8. The Administrative Order requires, among other things, that Gruntal and Gruntal Financial pay an aggregate of \$5.5 million in disgorgement and prejudgment interest to establish a fund (the "Fund") for the benefit of customers, states, and other third parties that are identified as due funds

from the Respondents as a result of the diversions of assets between 1984 and 1994.

9. In order to insure that the Fund is distributed fairly, timely, and in compliance with the procedures set forth in the Administrative Order, the Commission respectfully requests that the Court enter an Order establishing a disgorgement and distribution process administered by an independent person subject to the control of this Court.

Prayer for Relief

WHEREFORE, Petitioner Commission respectfully requests that this Court:

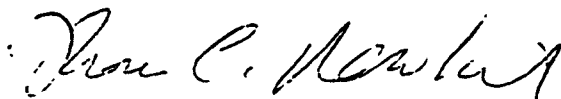
Issue an Order, pursuant to Section 20(c) of the Securities Act and Section 21(e) of the Exchange Act [15 U.S.C. §§ 77t(c) and 78u(e)]:

A. requiring Gruntal and Gruntal Financial each to comply with its obligations as set forth in the Administrative Order relating to the establishment of a disgorgement fund;

B. establishing a fund administered by an independent person subject to the control of this Court; and

C. granting such other equitable relief as the Court deems necessary or appropriate.

Respectfully submitted,



Dated: April 9, 1996

Thomas C. Newkirk (TN 7271)
Leo F. Orenstein
James T. Coffman
Antonia Chion
Jahan P. Raissi
David Frohlich

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UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION,	:	
	:	
Petitioner,	:	
	:	96 Civ.
v.	:	
	:	
GRUNTAL & CO., INCORPORATED	:	FINAL ORDER PURSUANT
	:	TO SECTION 20(c) OF THE
and GRUNTAL FINANCIAL CORP.,	:	SECURITIES ACT OF 1933
	:	AND SECTION 21(e) OF THE
Respondents.	:	THE SECURITIES EXCHANGE
	:	ACT OF 1934

Petitioner SECURITIES AND EXCHANGE COMMISSION ("COMMISSION"), having filed a PETITION FOR AN ORDER PURSUANT TO SECTION 20(c) OF THE SECURITIES ACT OF 1933 AND SECTION 21(e) OF THE SECURITIES EXCHANGE ACT OF 1934 ("PETITION"), and Respondents GRUNTAL & CO., INCORPORATED ("GRUNTAL") and GRUNTAL FINANCIAL CORP. ("GRUNTAL FINANCIAL"), in the attached CONSENT OF GRUNTAL & CO., INCORPORATED AND GRUNTAL FINANCIAL CORP. ("CONSENT"), which is incorporated herein, each having entered a general appearance, having admitted the jurisdiction of this Court over it and over the subject matter of this action, having waived the entry of findings of fact and conclusions of law pursuant to Rule 52 of the Federal Rules of Civil Procedure, and without prior trial, presentation of any evidence, or adjudication of any issue of law or fact, and without admitting or denying any of the allegations of the PETITION, having each consented to the entry of this FINAL ORDER, and it further appearing that this Court has jurisdiction over the parties and the subject matter hereof, and the Court being fully advised in the premises:

I. ORDER PURSUANT TO SECTION 20(c) OF THE SECURITIES ACT AND SECTION 21(e) OF THE EXCHANGE ACT

IT IS HEREBY ORDERED, ADJUDGED AND DECREED that, pursuant to Section 20(c) of the Securities Act of 1933 ("Securities Act") and Section 21(e) of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. §§ 77t(c) and 78u(e)], GRUNTAL and GRUNTAL FINANCIAL comply with all provisions relating to disgorgement and the distribution of such disgorgement in the COMMISSION's Order Instituting Public Administrative Proceedings, Making Findings, Imposing Remedial Sanctions, and Issuing Cease and Desist Order, Administrative Release No. (the "ADMINISTRATIVE ORDER") which was issued on April 9, 1996, in In the Matter of Gruntal & Co., Incorporated and Gruntal Financial Corp. GRUNTAL AND GRUNTAL FINANCIAL shall pay monies as set forth herein for the establishment of a disgorgement fund which, together with accrued interest (the "FUND"), is to be distributed pursuant to a plan under the direction of an independent fund administrator ("FUND ADMINISTRATOR"), as set forth in the ADMINISTRATIVE ORDER and this FINAL ORDER. The FUND shall be governed by the ADMINISTRATIVE ORDER, the PLAN OF DISTRIBUTION (described in Section II. below), and this FINAL ORDER.

II. FUND ADMINISTRATOR

Within 15 days of the entry of this FINAL ORDER, the COMMISSION shall recommend to the Court, with the consent of GRUNTAL and GRUNTAL FINANCIAL, which consent shall not unreasonably be withheld, a FUND ADMINISTRATOR. After considering the COMMISSION's recommendation, the Court shall

appoint and approve a FUND ADMINISTRATOR. Respondents shall, at Respondents' expense, retain the Fund Administrator appointed and approved by this Court. Within one year after the date of the ADMINISTRATIVE ORDER, the FUND ADMINISTRATOR shall submit a PLAN OF DISTRIBUTION, which shall be approved by this Court after an opportunity for interested parties to be heard, to disburse the monies in the FUND that is consistent with the terms of this FINAL ORDER and the ADMINISTRATIVE ORDER. The PLAN OF DISTRIBUTION, the ADMINISTRATIVE ORDER, and this FINAL ORDER shall govern the powers and duties of the FUND ADMINISTRATOR and the disbursement of monies in the FUND. The PLAN OF DISTRIBUTION shall be entered as a separate Order of this Court.

III. CREATION OF THE FUND

A. WHEREAS the COMMISSION has issued an ADMINISTRATIVE ORDER requiring GRUNTAL and GRUNTAL FINANCIAL to pay an aggregate of \$5.5 million for the benefit of customers, states, and other third parties that are identified as due funds from Respondents as a result of the diversions of assets between 1984 and 1994,

1. GRUNTAL and GRUNTAL FINANCIAL shall, within ten business days of the date of the ADMINISTRATIVE ORDER, deposit \$5.5 million in a Court Registry Investment System ("CRIS") account to be established in this case. These monies shall be distributed in accordance with this FINAL ORDER, the ADMINISTRATIVE ORDER, and the PLAN OF DISTRIBUTION.

a. Payment of this \$5.5 million shall be made into the registry of this Court by certified check or money order

drawn on a United States bank and made payable to "Clerk, United States District Court, S.D.N.Y." Upon receipt, the Financial Deputy Clerk shall deposit such check or money order into an interest bearing account with CRIS.

b. At the same time payment is remitted, GRUNTAL and GRUNTAL FINANCIAL shall send a photocopy of its check or money order to the Secretary of the COMMISSION at the following address:

Office of the Secretary
450 Fifth Street, N.W.
Mail Stop 6-9
Washington, D.C. 20549

The photocopy shall be accompanied by a letter that identifies GRUNTAL and GRUNTAL FINANCIAL as the Respondents in this action, the civil action number assigned to the case, the District Court in which the action and this FINAL ORDER were filed, and the COMMISSION internal case number (HO-2997). Copies of all such letters to the Secretary of the COMMISSION shall be sent simultaneously to counsel of record for the COMMISSION, Thomas C. Newkirk, Associate Director.

2. In the event that the FUND ADMINISTRATOR determines, pursuant to Section VI.A.3.(a) of this FINAL ORDER, that GRUNTAL has not repaid, recredited, escheated, or properly segregated and scheduled for escheatment \$6.7 million in connection with the conduct described in the ADMINISTRATIVE ORDER, GRUNTAL shall disgorge into the FUND the difference between \$6.7 million and the amount the FUND ADMINISTRATOR determines that GRUNTAL has actually repaid, recredited,

escheated, or properly segregated and scheduled for escheatment in connection with the conduct described in the ADMINISTRATIVE ORDER. Such additional disgorgement shall be distributed pursuant to the terms of the ADMINISTRATIVE ORDER, this FINAL ORDER, and the PLAN OF DISTRIBUTION that govern disbursements from the FUND.

3. If, as a result of research by Respondents or by the FUND ADMINISTRATOR, any of the amount referred to in Section VI.A.3.(a) of this ORDER which is segregated and scheduled for escheatment is determined not to be escheatable and is determined to belong to customers, contra-parties, vendors, or other third parties, then Respondents shall pay such monies to the parties to whom they belong. If at any time any of the amount referred to in Section VI.A.3.(a) of this FINAL ORDER which is segregated and scheduled for escheatment is determined not to be escheatable and not to be owed to customers, contra-parties, vendors, or other third parties, then Respondents shall pay such monies into the FUND and such monies shall be disbursed pursuant to the terms of the ADMINISTRATIVE ORDER, this FINAL ORDER, and the PLAN OF DISTRIBUTION that govern disbursements from the FUND.

4. Within one year after the date of the ADMINISTRATIVE ORDER, the FUND ADMINISTRATOR shall submit a PLAN OF DISTRIBUTION to disburse the monies in the FUND. After an opportunity for interested parties to be heard and upon approval of the PLAN OF DISTRIBUTION by this Court, the FUND ADMINISTRATOR

shall disburse the monies in the FUND. Any residual amount shall go to the United States Treasury.

5. Under no circumstances shall any of the assets in the FUND be paid to or revert to Respondents, their assigns, subsidiaries, or shareholder(s).

IV. USES OF THE FUND

A. The FUND established pursuant to Section III.A. above shall be used for the benefit of customers, contra-parties, vendors, states, and other third parties that are identified by the FUND ADMINISTRATOR as due funds from Respondents as a result of the diversions of assets between 1984 and 1994. The FUND is to be disbursed as follows:

1. first, to pay any taxes on the income earned on the FUND,
2. second, to repay to customers such monies identified as owing to them,
3. third, to repay to vendors, contra-parties, and other third parties such monies identified as owing to them,
4. fourth, to escheat to the proper state(s) such monies identified as presently escheatable,
5. fifth, to have assets identified as potentially escheatable, but not yet ripe for escheatment, properly maintained in segregated accounts until escheated, and
6. sixth, to pay any residual balance into the United States Treasury.

B. The FUND is intended to be a "qualified settlement fund" within the meaning of regulations issued under Section 468B(g) of the Internal Revenue Code of 1986, as amended. The FUND ADMINISTRATOR is designated the administrator of the FUND, pursuant to Treas. Reg. § 1.468B-2(k)(3)(i) and shall satisfy the administrative requirements imposed by Treas. Reg. § 1.468B-2, including but not limited to (1) obtaining a taxpayer identification number, (2) timely filing applicable tax returns and paying taxes reported thereon, and (3) satisfying any information reporting or withholding requirement imposed on distributions from the FUND. GRUNTAL and GRUNTAL FINANCIAL shall each provide the FUND ADMINISTRATOR with all relevant information and otherwise cooperate with the FUND ADMINISTRATOR in fulfilling the FUND's obligations under Treas. Reg. § 1.468B-2.

V. RESTRICTIONS ON PAYMENTS FROM THE FUND

A. The FUND shall not be used to pay:

1. any judgment or award of punitive or non-compensatory damages arising out of the diversions of assets;
2. any fees, costs, and expenses incurred by the FUND ADMINISTRATOR in connection with and incidental to the performance of his or her duties under this FINAL ORDER, including the compensation of the FUND ADMINISTRATOR, and the fees, costs, and expenses of any persons engaged to assist him or her; or
3. any amount denominated as attorneys' fees, costs, or disbursements.

VI. FUND ADMINISTRATOR

A. The FUND ADMINISTRATOR shall:

1. have all appropriate powers and authority to perform his or her duties as set forth in this FINAL ORDER and the ADMINISTRATIVE ORDER, including, without limitation, the powers to hire such persons as are reasonably necessary to perform his or her duties as set forth in this FINAL ORDER and the ADMINISTRATIVE ORDER;
2. file tax returns on behalf of the FUND;
3. conduct such investigation, research, and review as is necessary and practicable to: (a) verify GRUNTAL's representation to the COMMISSION that it has repaid, recredited, escheated, or properly segregated and scheduled for escheatment \$6.7 million which it has identified as escheatable, or presently believes to be escheatable, or has identified as belonging to customers, contra-parties, vendors, and other third parties, in connection with the conduct described in the ADMINISTRATIVE ORDER, and (b) where practical, identify the type (e.g., dividends), ownership (e.g., customer), and nature (e.g., escheatable) of the assets diverted in connection with the diversions of assets between 1984 and 1994 as described in the ADMINISTRATIVE ORDER, which are presently so unidentified;
4. following such investigation and research, but in any event no later than one year after the date of the ADMINISTRATIVE ORDER, submit to this Court, the Director of the Division of Enforcement of the COMMISSION, and the Respondents:

(a) a report of his or her findings, and (b) a PLAN OF DISTRIBUTION to disburse the FUND in accordance with this FINAL ORDER and the ADMINISTRATIVE ORDER;

5. after an opportunity for interested parties to be heard, and upon approval of the PLAN OF DISTRIBUTION by this Court, disburse the funds in accordance with the PLAN OF DISTRIBUTION;

6. be entitled, to the extent he or she deems appropriate, to rely upon work performed or to be performed by Ernst & Young LLP, Deloitte & Touche LLP, GRUNTAL's Quality Assurance Task Force, GRUNTAL's Operations Division, and GRUNTAL's Operations Control Group; and

7. be entitled, to the extent that he or she deems appropriate, to require GRUNTAL to continue the engagement of Deloitte & Touche LLP and to maintain resources within its Operations Control Group to support the efforts of the FUND ADMINISTRATOR.

B. The FUND ADMINISTRATOR and his or her agents and attorneys shall be indemnified and held harmless against all liabilities, claims, and demands arising from or relating to any act or omission to act in the course of performing his or her duties, except to the extent that this Court finds that such person acted in bad faith, gross negligence, reckless disregard of his or her duties, or in a manner that he or she knew was contrary to the terms of this FINAL ORDER or the ADMINISTRATIVE ORDER.

C. The FUND ADMINISTRATOR shall not, without the prior written consent of the Director of the Division of Enforcement of the COMMISSION, enter into any legal, business, or other financial relationship with GRUNTAL or GRUNTAL FINANCIAL, other than as described in this FINAL ORDER and the ADMINISTRATIVE ORDER, for the period of the engagement and for a period of two years following the completion of his or her duties described in this FINAL ORDER.

D. If the FUND ADMINISTRATOR resigns or is otherwise unable to serve, the COMMISSION shall recommend to the Court a successor, with the consent of the Respondents, which consent shall not unreasonably be withheld. After considering the COMMISSION's recommendation, the Court shall appoint and approve a successor. Respondents shall retain, at Respondents' expense, the successor appointed and approved by this Court within 30 days after the appointment and approval of such successor. All provisions in this FINAL ORDER that apply to the FUND ADMINISTRATOR shall apply to any successor.

VII. DUTIES OF GRUNTAL AND GRUNTAL FINANCIAL TO THE FUND ADMINISTRATOR

GRUNTAL and GRUNTAL FINANCIAL each shall:

A. Cooperate fully with the FUND ADMINISTRATOR, including using all reasonable efforts to obtain the cooperation of Respondents' employees or other persons under their control, including Ernst & Young LLP and Deloitte & Touche LLP, and giving the FUND ADMINISTRATOR full access to all documents and premises under the Respondents' control.

B. Compensate the FUND ADMINISTRATOR and persons engaged to assist the FUND ADMINISTRATOR for services rendered pursuant to this FINAL ORDER and the ADMINISTRATIVE ORDER at their reasonable and customary rates.

C. Indemnify, defend, and hold harmless the FUND ADMINISTRATOR and his or her agents and attorneys from and against all liabilities, claims, and demands arising from or relating to any act or omission to act in the course of performing his or her duties, except to the extent that the Court finds that such person acted in bad faith, gross negligence, reckless disregard of his or her duties, or in a manner that he or she knew was contrary to the terms of this FINAL ORDER or the ADMINISTRATIVE ORDER.

D. Not be in and shall not have an attorney-client relationship with the FUND ADMINISTRATOR and shall not seek to invoke the attorney-client or any other doctrine or privilege to prevent the FUND ADMINISTRATOR from transmitting any information, reports, or documents to the Court, the COMMISSION, or its staff.

E. Not, without the prior written consent of the Director of the Division of Enforcement of the COMMISSION, enter into any legal, business, or other financial relationship with any firm with which the FUND ADMINISTRATOR is affiliated or of which he or she is a member, and any person engaged by the FUND ADMINISTRATOR to assist the FUND ADMINISTRATOR in the performance of his or her duties under this FINAL ORDER, other than as described in this FINAL ORDER and the ADMINISTRATIVE ORDER, for the period of their

engagements and for a period of two years following the completion of their duties described in this FINAL ORDER.

VIII. STANDING

Nothing herein shall be deemed to confer standing upon any persons other than the COMMISSION, GRUNTAL, GRUNTAL FINANCIAL, and the FUND ADMINISTRATOR.

IX. NO COMPROMISE, SETTLEMENT OR ADJUDICATION OF CLAIMS

Nothing herein is intended to or shall be construed to have created, compromised, settled, or adjudicated any claims, causes of action, or rights of any person whomsoever, other than as between the COMMISSION and GRUNTAL and GRUNTAL FINANCIAL, in accordance with their Consent.

X. COURT RETAINS JURISDICTION

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that this Court shall retain jurisdiction of this action for all purposes, including implementation and enforcement of this FINAL ORDER.

Dated: _____

UNITED STATES DISTRICT JUDGE