ADMINISTRATIVE PROCEEDING
FILE NO. 3-2606

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of	:	
IRWIN L. GERMAISE and THOMAS F. QUINN	:	(Private Proceeding)
Rule 2(e) of the Rules of Practice	:	

INITIAL DECISION

October 29, 1971
Washington, D.C.

David J. Markun
Hearing Examiner

C O N T E N T S

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APPEARANCES: Robert E. Kushner, Assistant General Counsel and Patricia H. Latham, Attorney, for the Office of General Counsel, with Walter P. North, Associate General Counsel, and Frederick T. Spindel, Attorney, also appearing on the brief.

Irwin L. Germaise, Esquire and Thomas F. Quinn, Esquire, of New York, New York, appearing pro se.

BEFORE: David J. Markun, Hearing Examiner

THE PROCEEDING

This private proceeding was instituted by an order of the Commission dated September 8, 1970, pursuant to Rule 2(e) of the Commission's Rules of Practice, 17 CFR 201.2(e), to determine whether the charges of unethical and improper professional conduct reflected in the order for proceeding against the respondents, Erwin L. Germaise and Thomas F. Quinn, attorneys at law, are true, and, if so, whether the respondents should be temporarily or permanently disqualified from practicing law before the Commission.

The hearing in this proceeding took place in Washington, D.C., on January 25th through the 28th, 1971, with respondents appearing pro se. As part of the post-hearing procedures, proposed findings, conclusions, and supporting briefs were filed by the parties.

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

FINDINGS OF FACT AND LAW

The Charges; Findings

Respondents Irwin L. Germaise ("Germaise") and Thomas F. Quinn ("Quinn") are partners in the law firm of Germaise and Quinn (formerly Germaise, Cooper [1/] & Quinn) at 717 Fifth Avenue in New York, New York.

Germaise, 41, has been practicing law since his admission to practice in the State of New York in 1955. His practice has involved

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1/ Jerome Cooper ("Cooper") left the law partnership in mid-September, 1969.

a particular emphasis on securities-law matters, and he has represented clients in numerous public offerings of securities.[2/]

Quinn, 34, was admitted to practice in the State of New York in 1962 and has practiced before the Commission. In the latter part of 1962 and during a part of 1963 Quinn was president of Thomas Williams & Lee, Inc., a broker-dealer firm.

The charges in this proceeding arise out of Germaise's representation of Bagels, U.S.A., Inc. ("Bagels") in a Regulation A offering[3/] of its securities under Section 3(b) of the Securities Act of 1933, 15 U.S.C. 77c(b), and Quinn's representation of Monarch Funding Corp. ("Monarch"), the underwriter involved in the offering.

It is alleged in essence that respondents in connection with the Bagels offering made or allowed to be made untrue and misleading statements of material fact.[4/] In particular, it is alleged, among other things, that respondents failed to disclose to the underwriter, the Commission, or the public that they were partners in the practice of law at the time of the Bagels offering; that they failed to disclose various loans to Bagels, the issuer, which should have been disclosed; and that they failed to describe accurately the purposes for which the proceeds of the offering were to be used.

2/ His experience includes 3 years of employment with the Commission.

3/ The offer of securities in a Regulation A offering involves filing with the Commission a notification, offering circular, and other exhibits related to the proposed offering; these filings are required in order to afford an exemption from the registration requirements of the Securities Act of 1933, in accordance with Rules 255 and 256, 17 CFR 230.255 and 230.256.

4/ Paragraph 7 of the order for proceeding alleges as follows:

(Continued)

The order alleges that such alleged conduct, coupled in the case of respondent Quinn with his criminal conviction in the United States

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4/ (Continued)

"7. The aforesaid misstatements and omissions of material fact included the following:

"(a) The offering circular and notification, as amended, represented that legal matters in connection with the offering had been passed upon for the issuer by respondent Germaise, and for the underwriter by respondent Quinn. A separate address was given for each respondent. In making these statements, which in effect represented that the issuer and the underwriter each had separate and independent counsel, respondents Germaise and Quinn omitted to state that they were in fact copartners in the practice of law and that legal fees earned from the offering would be placed in the partnership account.

"(b) Respondent Germaise caused Monarch, the underwriter, to retain respondent Quinn as its counsel in connection with the Bagels offering, but both respondents failed to disclose their partnership to Monarch.

"(c) The Bagels notification and offering circular, as amended, represented that (1) except as disclosed therein there had been no material transactions between Bagels and its officers, directors or promoters; and (2) there were no amounts due to or from Bagels and its officers and directors. These statements were untrue and misleading because they failed to disclose:

(i) loans of $20,000 made to Bagels by Kathleen Sidoti, a director; and

(ii) a loan of $10,000 made to Bagels by Jerome Cooper, respondents' copartner and a promote of Bagels.

"(d) The offering circular of Bagels, as amended, failed to disclose a loan of $15,000 owed by Bagels to Trade Bank and Trust Company, and personally guaranteed by Harold Glantz and Arthur Goldberg, officers and shareholders of Bagels.

"(e) The offering circular of Bagels failed to disclose that Bagels had contracted to purchase, for $60,000, a real property used for bagel manufacture and retail sales, and had also contracted to purchase for some $15,000, machinery, equipment and merchandise located on said property.

"(f) The offering circular of Bagels, as amended, failed to describe accurately the purposes for which the proceeds of the stock offering would be used. The amount of proceeds to be applied in repayment of loans was stated to be $10,000, while the actual amount was $45,000 (see ¶7(c), (d), above). Further, the application of proceeds section wholly failed to take into account the proceeds to be used for the purchase of the real property and machinery, merchandise and equipment discussed in the preceding paragraph (¶7(e)).

(Continued)

District Court for the Southern District of New York for violations of the registration and antifraud provisions of the Securities Act of 1933 ("Securities Act") [5/] establishes within the meaning of Rule 2(e) of the Commission's Rules of Practice that respondents do not possess the requisite qualifications to represent others, are lacking in character and integrity and have engaged in unethical and improper professional conduct.

The evidence establishes that in late August or early September of 1968 Jerome Cooper ("Cooper"), who was later to become a law partner of respondents Germaise and Quinn, introduced to Germaise at his office a businessman named Harold Glantz ("Glantz") [6/] who wanted to explore the possibilities with Germaise of a public offering of securities by one or more of Glantz's business activities. After discussing the feasibility of taking public the various business activities (pants, plastics, and bagels) in which Glantz had an interest, it appeared to him and to Germaise that Bagels offered the only suitable prospect for a public offering. Germaise pointed out to Glantz that he would need an underwriter for the contemplated offering.

4/ (Continued)
"(g) The notification and offering circular of Bagels, as amended, represented that from June 1966 until October 4, 1968, Harold Glantz, the company's president and treasurer, and Arthur Goldberg, its vice-president and secretary, owned all of the outstanding capital stock of the ten subsidiary corporations of Bagels. In fact, substantial shareholdings were in the hands of other persons during that time period, and the identities of, and shares held by, such persons were not disclosed."

5/ The conviction on July 31, 1970, in the U.S. District for the Southern District of New York, was affirmed by the Court of Appeals for the Second Circuit on June 4, 1971.

6/ Cooper had known Glantz since 1962, had performed legal services for him, and was on good personal terms with him. They were joint owners of certain property.

Thereafter, in September of 1968, Glantz suggested to Germaise the names of some prospective underwriters which he had obtained from a broker-dealer. Germaise indicated that of those mentioned he preferred Monarch, and Glantz accepted that preference. Germaise then telephoned Leo Eisenberg, ("Eisenberg") president of Monarch, to tell him of Glantz's desire that Monarch serve as underwriter, and at the same time requested that Eisenberg have Monarch retain respondent Quinn, to whom Germaise considered he "owed a referral", as counsel representing the underwriter. Eisenberg agreed to do so.

Germaise arranged for the incorporation of Bagels as a new corporation in the State of Florida on October 3, 1968, utilizing the services of United States Corporation Company. The new entity then acquired the shares of ten predecessor corporations owned by Glantz and others which were already engaged in the bagels business in New Jersey, New York, and Ohio.

On November 1, 1968, Germaise, on behalf of Bagels, filed with the Commission's regional office in Atlanta, Georgia, a notification, offering circular and exhibits relating to a proposed Regulation A offering of 60,000 shares of the common stock of Bagels at $5 per share. On November 29, 1968, Germaise filed an amended offering circular with the Atlanta Regional Office and on December 20, 1968, he filed definitive copies of the offering circular. The offering of the Bagels stock commenced December 27, 1968, and was completed [7/] sometime in January, 1969.

7/ The exemption of Bagels under Regulation A was temporarily and then permanently suspended by the Commission. Ad. Proc. File No. 3-2303, order of 1-27-70; Securities Act Release No. 5079, August 14, 1970 (Exhibits 49, 50). In reaching the findings and conclusions made herein, no reliance is placed upon these suspensions by the Commission.

The net proceeds of the offering, amounting to $264,000, were deposited in Bagels' checking account at the Trade Bank and Trust Co. ("Trade Bank") on January 20, 1969.

The notification under Regulation A filed by Germaise on November 1, 1968, identified counsel for the issuer and the underwriter as follows:

"Item 4. Counsel for Issuer and Underwriter

"Counsel for Issuer:
Irwin L. Germaise
59 East 54th Street
New York, New York 10022

"Counsel for Underwriter
Thomas F. Quinn
299 Broadway
New York, New York"

The offering circular filed by Germaise on November 1, 1968, stated as follows:

"LEGAL MATTERS

"Legal matters in connection with this offering have been passed on by Irwin L. Germaise, Esq., 59 East 54th Street, New York, New York, and for the Underwriter by Thomas F. Quinn, Esq., 299 Broadway, New York, New York."

While the notification and offering circular were amended in several respects by the amendments filed on November 29, 1968, and while the offering circular was again amended in limited respects by the definitive copy of the offering circular filed December 20, 1968, the portions of the notification and offering circular set forth above remained unchanged except that the definitive copy of the offering circular filed on

December 20, 1968, effected a minor clarifying addition.[8/]

The representations made in the notification and the offering circular as to the performance of legal services by the respondents in connection with the Bagels Regulation A offering were materially misleading because they failed to disclose the highly material fact that by mid-November of 1968 (if not earlier) the respondents, together with Cooper, were partners in the practice of law, with offices at 717 5th Avenue, New York, New York.

While the partnership agreement was oral rather than written and while respondents and Cooper testified that it was their "intention" to begin their partnership at about the first of the year 1969, the evidence is overwhelming that in fact the law partnership was in existence and functioning at least by mid-November of 1968.[9/]

Discussions looking to a three-member partnership began sometime in October, 1968. Although Germaise had known Cooper for 25 years[10/] and Quinn for some 8 years, it was the pendency of the proposed Bagels offering that brought the three together in a close professional relationship. Glantz, who already knew Cooper well, also became a social friend

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8/ The "Legal Matters" section, as modified with the addition of new language (underscored below) and the deletion of bracketed language provided as follows:

> "Legal matters in connection with this offering have been passed [on] upon for the company by Irwin L. Germaise, Esq., 59 East 54th Street, New York, New York, and for the Underwriter by Thomas F. Quinn, Esq., 299 Broadway, New York, New York."

9/ Respondents concede in their brief at p. 271, in their proposed findings, that a "partnership de facto" was formed by the three partners "in the latter part of November, 1968."

10/ Germaise and Cooper attended both high school and law school together.

of Quinn's [11] and encouraged the idea of a law partnership.

On November 1, 1968, Cooper on behalf of the partnership took an assignment from Marshall Leeman & Co., Inc. ("Marshall Leeman") of a sublease of office space at 717 Fifth Avenue subject to the approval of John Blair & Co., the sublessor. [12] The partnership also agreed to purchase Marshall Leeman's office furniture and equipment and to reimburse it for rental security it had deposited in the sum of some $22,000.

Cooper and Quinn moved into the partnership office space at 717 Fifth Avenue in the beginning of November. [13] Germaise, however, had some problems in closing down his 54th Street office, in addition to which suitable permanent office space for him at the partnership office was not available until Marshall Leeman moved out entirely at the end of December. [14] As a result, Germaise did not physically move to the partnership offices until the beginning of January, 1969. However, Germaise did perform partnership work at the partnership premises (as well as at his old office) during November and December of 1968, during which period he alternated between the partnership offices and his

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11/ Quinn and Glantz discovered they lived relatively close to one another and sometimes drove to town together. They and their wives were social friends.

12/ On November 19, 1968, the sublessor approved the partnership's subtenancy and the partnership promptly paid the November rent. The sublease covered 4,000 sq. feet at an annual rental of $47,092.59. Marshall Leeman was to retain 2,000 sq. ft. of the space until it moved out completely at the end of December, 1968.

13/ The record is not clear whether Quinn retained the use of any office space at his old offices at lower Broadway during November and December but the record is clear that the bulk of his time during that period was spent at the partnership offices at 717 Fifth Avenue.

14/ See footnote 12 above.

54th Street office, which were only a short walking distance apart.

On November 12, 1968, the partnership opened a checking account at Trade Bank at which time Germaise, Cooper, and Quinn each certified to the bank that "they are general partners, conducting business under the firm name and style of Germaise, Cooper and Quinn, Attorneys at 717 5th Avenue, New York, New York." 15/

The partnership began generating revenue in mid-November 1968. At least $5,000 in partnership fees was received in November and in the following month the partnership received at least $38,000 in fees. 16/ The partnership in November and December achieved a success that was well beyond the expectations of the partners.

Each of the three partners performed partnership work during the November-December period and each made "draws" 17/ on the revenues generated during that period.

Thus, although the partnership did not obtain its stationery until December and did not send out announcements of its formation until the third week of December, 18/ it is clear on the basis of the facts found

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15/ During November 1968 the account showed deposits totaling $15,298.04 and check withdrawals of $14,099.91. In December deposits totaled $38,076.58 and withdrawals $22,819.02.

16/ Many of the clients had been brought in as partnership clients by Germaise. During this November-December period the partnership had one full-time clerical employee and a part time typist and also utilized the secretaries at Green Bus Lines (See footnote 17).

17/ For purposes of dividing equally the partnership's net income Cooper's salary ($350 per month) from Green Bus Lines (by which he continued to be employed as an individual so that he could continue to participate in various employment benefits) was treated as if it were partnership income.

18/ Partnership records indicate a phone was connected December 9, 1968.

above that the partnership had been formed and was functioning at least by mid-November of 1968.[19/]

The existence of the three-member law partnership was a material fact[20/] that Germaise and Quinn should have made certain was disclosed in the notification and in the offering circular. Disclosure in the offering circular was necessary to put the prospective purchaser on notice that the existence of the partnership established a potential conflict of interest that might have affected the ability of Quinn to perform objectively and independently the usual independent investigation performed on behalf of the underwriter.[21/] Failure to disclose the partnership in the notification filed with the Commission under Regulation A,[22/] which requires disclosure of the names and addresses of counsel, misled the Commission and also potentially misled prospective investors, since the notification is a public document available for examination by the public.

19/ In re Lichtbau, 261 N.Y.S. 863 (Surr. Ct. Bronx Cty, 1933).

20/ Under the federal securities laws the basic test as to whether particular facts are material and must therefore be properly disclosed to investors is "whether a reasonable man would attach importance . . . [to them] in determining his choice of action in the transaction in question." S.E.C. v. Texas Gulf Sulphur Co., 401 F.2d 833 (C.A. 2, 1968) cert. den. sub. nom. Kline v. S.E.C., 394 U.S. 976 (1969); List v. Fashion Park, Inc., 340 F.2d 457, 462 (C.A. 2), cert. den. 382 U.S. 811 (1965).

21/ Respondents make the argument that the Commission's regulations do not call for designation in the offering circular of the identity of counsel for the issuer or the underwriter and that therefore the identity of counsel cannot be a material fact. This argument overlooks the point that by volunteering information concerning the identity of legal counsel (whether out of "egotism" or to "get some advertising", as Germaise suggested, or for whatever reason) they invited the potential investor to treat the information as relevant and had an obligation to make full disclosure of the facts. Moreover, in an analogous situation, the Commission has long taken the position that a misstatement in a registration statement may be material and result in a stop order even though it was volunteered by the registrant and not required to be included in the registration statement. Central Specialty Co., 10 SEC 1094, 1098 (1942); Southeastern Industrial Loan Co., 10 SEC 617, 631-32- (1941).

22/ Form 1-A, Item 4, pursuant to Regulation A.

Respondents argue at great length, but mistakenly, that they were under no duty to disclose the existence of the partnership because in fact Germaise and Quinn each performed his services independently of one another for the issuer and for the underwriter, respectively, and not as a partnership matter.[23/] This argument misses the whole point, which is that the public and the Commission are entitled to know that individual members of a law partnership are representing the issuer and the underwriter, respectively, even where they do so "independently" as individuals and not on behalf of the partnership, so that the Commission and prospective investors may for themselves conclude, based on a full disclosure of the facts,[24/] whether the existence of the law partnership establishes a relationship that would adversely affect the capacity of the individual

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23/ The record establishes that, with one exception, the legal work that was done was done by Germaise for the issuer and by Quinn for the underwriter. The "exception" involved an instance in which Cooper, at Quinn's request and in his stead, attended a "due diligence" meeting at the Commission's offices in New York, New York, on behalf of the underwriter, though the underwriter was not aware that Cooper was appearing on his behalf and assumed he (Cooper) was representing the issuer! The record further shows that the $2500 fee paid to Quinn by the underwriter was contributed to partnership revenues. Of the $7,500 in legal fees paid by the issuer, the first $3,000, paid on October 31, 1968, before the partnership was formed, was paid to and kept by Germaise individually. After the partnership was formed, Bagels paid $1,000 on account by check in favor of the partnership on November 18, 1968 (when the partnership was in need of starting-up funds) and the final payment of $3,500 was paid by a check to Germaise dated January 20, 1969, which he deposited in the partnership account. The partners testified that of the $7,500 fee paid by Bagels, Germaise owed Cooper $2,500 as a referral fee (though Cooper performed no services other than occasionally to "get some information" from Glantz) and that in effect capital contributions were made by the partners of their fees stemming from the Bagels offering in the following amounts: Quinn, $2,000; Cooper, $2,500; and Germaise, $2,000. However, respondents produced no partnership books to establish that the fees were treated as capital contributions.

24/ In this connection, full disclosure in the instant case would have required an indication as to how the legal fees were being deposited. See footnote 23 above.

attorneys to exercise sound independent judgment.[25/]

Respondents also failed, as charged, to advise the underwriter of their law partnership. Eisenberg, president of the underwriter, testified that he did not learn of the partnership until the end of February or the beginning of March, 1969.[26/] Quinn testified that "sometime" in December of 1968 he told Eisenberg that he "was contemplating going into a partnership with Mr. Germaise and Mr. Cooper," but Eisenberg did not recall being so informed. Resolving this doubt in Quinn's favor is of no benefit to him here since by advising Eisenberg in December that he "contemplated" going into the partnership he was misinforming him rather than informing him since the partnership had already been formed and was functioning by mid-November of 1968.

By failing to advise the underwriter[27/] of their partnership the respondents came into violation of Canon 6 of the Canons of Professional Ethics of the American Bar Association, which provided in part that:[28/]

> "It is the duty of the lawyer at the time of retainer to disclose to the client all the circumstances of his relations to the parties, and any interest in or connection with the controversy, which might influence the client in the selection of counsel.

25/ See W.E. Bassett Co. v. H.C. Cook Co., 201 F. Supp. 821 (D. Conn.) aff'd per curiam, 302 F.2d 268 (C.A. 2, 1962), where an attorney was disqualified from privately representing a client because a partner in the law firm he had joined had formerly represented a client with adverse interests.

26/ He also testified that he had no recollection of having received an announcement of the formation of the law firm when they were sent out in the third week of December, 1968, and there is no satisfactory proof that he did receive one.

27/ The issuer, of course, through its president, Glantz, was well aware of the partnership between Germaise, Cooper, and Quinn and had, in fact, as already noted, encouraged its formation.

28/ Martindale-Hubbel Law Directory, 1969, Vol. III, p. 197A. For comparable provisions in the new Code of Professional Responsibility, effective January 1, 1970, see Canon 5 and disciplinary rules DR 5-101A, DR 5-105.

"It is unprofessional to represent conflicting interests, except by express consent of all concerned given after a full disclosure of the facts . . . ."

This Canon applies to situations where the parties have a potential conflict of interests as well as to cases where there is an actual and present conflict. 29/

Although an issuer and an underwriter in an offering of securities have a common interest in that both seek to effect a distribution and sale of the securities, nevertheless there exist between them a number of potentially conflicting interests that make considerations reflected in Canon 6 applicable. Thus, the issuer and underwriter could come into conflict over the nature and terms of the underwriting agreement. In addition, the underwriter is subject to civil liability or injunctive action for material misrepresentations or omissions under various provisions of the Securities laws 30/ and may well be more concerned than the issuer 31/ to avoid violation of such provisions.

The respondents never gave the underwriter a chance to decide for itself on the basis of all material facts whether it wanted to continue to engage Quinn as its attorney in light of his having become a partner of Germaise and Cooper in mid-November. Their failure to have informed Eisenberg is perhaps even more culpable here in view of the fact that it

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29/ In re Kamp, 40 N.J. 558, 194 A.2d 236 (1963); Kelly v. Greason, 23 N.Y. 2d 368, 296 N.Y.S. 2d 937, 244 N.E. 2d 456 (1968).

30/ E.g. 15 U.S.C. 77l(2); 15 U.S.C. 77q(a); 15 U.S.C. 78j(b).

31/ The issuer, too, is subject to potential liabilities and sanctions, but he may be more disposed to take greater risks than the underwriter because of the issuer's more direct interest in the distribution whereas the long-range concern of the underwriter to stay in business can generally be counted on by the Commission and the public to make him more cautious.

was Germaise who recommended the engagement of Quinn by the underwriter.[32]

These omissions by respondents to disclose their partnership to the Commission, the underwriter, and the public were not the result of inadvertence but rather of quite deliberate decision. Thus, the record discloses that sometime between approximately November 29, 1968 and December 17, 1968, Germaise and Quinn together specifically considered the question of whether their law partnership relationship should be disclosed. They testified that they concluded it need not be disclosed because they would each continue to act independently and because they did not "intend" the partnership to commence until the beginning of January, 1969.[33] Neither stated reason for the decision not to disclose is valid, since, as already concluded above, there was a duty to disclose the existence of the partnership even though each continued to act independently, and, concerning the latter stated basis, a valid partnership had in fact been formed by mid-November.

Apart from the failure to disclose the existence of the law partnership, a number of other misrepresentations of, or omissions to state, material facts, as charged, occurred in connection with the Bagels offering.

The offering circular under "Certain Transactions with Management" stated: "Except as herein disclosed, there have been no material transactions between the company and its officers, directors, promoters or affiliates and none are contemplated." Footnote 7 to the financial

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32/ It may be that, paradoxically, it was the very fact that Germaise had recommended Quinn to Eisenberg that made respondents reluctant to disclose their law partnership when they specifically considered the need for such disclosure, as discussed in the text immediately following.

33/ From their consultation together it follows that both respondents must share equally the blame for failure to make the required disclosures.

statements[34] declared: "There are no amounts due to or from officers, directors and promoters." Under "Application of Proceeds" the sum of $10,000 was designated as being to "Repay Loan".

The record establishes that in fact there were loans totaling $30,000 which should have been disclosed under "Certain Transactions With Management" and loans totaling $45,000[35] which should have been disclosed under "Application of Proceeds."

Cooper, respondents' law partner, was a promoter and shareholder of Bagels. He lent Bagels $10,000 on October 5, 1968, and was repaid from the proceeds of the offering by a check dated January 22, 1969. Kathleen Sidoti, a director and holder of 100,000 shares of Bagels, made two $10,000 loans to Bagels on December 3, 1968, and January 2, 1969, and was repaid the $20,000 from the proceeds of the Bagels offering by check dated January 20, 1969.

On November 15, 1968, Bagels borrowed $15,000 from the Trade Bank under a loan guaranteed by Glantz and Arthur Goldberg ("Goldberg"), the president-treasurer and vice president-secretary, respectively, of Bagels. The loan was due in two months and was repaid on January 21, 1969, from the proceeds of the offering.

Germaise concedes he knew of the Cooper loan to Bagels, and Quinn admits that he knew of the Trade Bank loan to Bagels. Although the

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34/ This footnote was in response to a letter of comment dated November 12, 1968, by the Commission's Atlanta Regional Office, which stated that "[a]mounts due to or from officers, directors and promoters, if any, should be stated separately in the balance sheet."

35/ As noted above, the "Application of Proceeds" entry indicated that only a $10,000 loan was to be repaid out of the proceeds of the offering, thus understating the correct figure by $35,000.

respondents had a number of discussions respecting the Bagels offering they evidently failed to pool their knowledge respecting the outstanding loans or to consult their co-law partner, Cooper, a close friend of Glantz's and knowledgeable respecting Bagels.

Germaise never saw fit to inquire specifically of Glantz or Goldberg as to the existence of any loans that would have to be disclosed. Indeed, so casual and inadequate was Germaise's inquiry and instruction in this regard that Glantz testified that it was his understanding that no matters occurring subsequent to August 31, 1968 — the date of the financial statements prepared for the offering — needed to be disclosed.

This understatement by $35,000 of the loans to be repaid out of the proceeds of the offering misrepresented a material fact. The $35,000 figure was over 13% of the net proceeds ($264,000) of the offering and exceeded substantially Bagels' reported net income of $26,821 for the six months ended 8-31-68.

In addition, the offering circular failed to disclose that on December 26, 1968, Bagels had entered into a contract to purchase real property in the Bronx for $60,000. A down payment of $6,000 was made at the time and the balance was payable at the closing, scheduled for February 10, 1969. The building had previously been used in bagels manufacturing and contained necessary equipment. Shortly before, Bagels had purchased some automatic baking equipment that was on the premises and later used over $10,000 from the proceeds of the offering to pay for the equipment.

The offering circular, which became effective on December 27, 1968, made no mention of the contract to purchase the realty or of the recent purchase of equipment. The offering circular described a "Northern Commissary" located in Bergenfield, New Jersey, which was said to fulfill the company's manufacturing needs in the North, and a proposed "Southern Commissary" which was to be established from a portion of the proceeds of the offering and was to service the company's prospective southern manufacturing needs. This presentation was misleading since disclosure of the $60,000 contract for purchase of the property in the Bronx and the recent purchase of equipment there might have raised considerable doubt as to the adequacy of the "Northern Commissary" in Bergenfield, New Jersey.

Cooper and Quinn were well aware of the $60,000 contract since Cooper represented Bagels in the matter and Quinn had twice (unsuccessfully) tried to get the owner to lease the premises to Bagels. Germaise, who testified he was not aware of the contract, would have known of it had he properly instructed Glantz and Goldberg as to what had to be disclosed and had made suitable inquiry.

The Bagels offering circular also falsely stated that from June 1966 until October 4, 1968, Glantz and Goldberg owned all of the stock of the 10 bagels firms that were acquired by Bagels in 1968 whereas in fact other persons held substantial amounts of stock in at least seven of the subsidiaries during that time period.

Quinn admitted he knew of such other shareholders and Germaise, who denied such knowledge, should have known, for the information was readily available to him from the minute books and stock records of the subsidiary

companies, all but two of which were in his office prior to December 27, 1968, when the offering became effective.

The representation as to ownership, not required by any law or regulation, was misleading in that it tended to create a false picture of stability and continuity in the bagels operation and ownership.

As to respondent Quinn, the order for proceeding alleges as an additional basis for disciplinary action against him his conviction on July 31, 1970, in the United States District Court for the Southern District of New York [36/] of violations of the registration and antifraud provisions of the Securities Act of 1933. [37/] The indictment charged, and the judgment of conviction determined, that in 1963 Quinn, in connection with the securities of Kent Industries, Inc., engaged in an unlawful scheme to sell unregistered shares of stock, made false and fraudulent representations of material facts and omitted to disclose material facts to purchasers of Kent Industries, Inc. securities. Quinn's conviction was affirmed by the Court of Appeals for the Second Circuit on June 4, 1971. [38/] The Court of Appeals opinion describes Quinn as the "moving spirit" of Thomas, Williams & Lee, Inc., the brokerage firm that served as the vehicle for the fraudulent sales of Kent Industries stock.

36/ See footnote 5 above and footnote 38 below.

37/ Sections 5(a), 17(a) and 24 of the Securities Act of 1933, 15 U.S.C. 77e(a), 77q(a) and 77x. Section 24 of the Act provides that any person who wilfully violates any provision of the Act shall upon conviction be fined not more than $5,000 or imprisoned not more than five years, or both. This makes violations of the Act a felony. 18 U.S.C. 1.

38/ United States v. Thomas F. Quinn, David Gennaro and Gary Seiden, (C.A. 2d, 6-4-71), Docket Nos. 35471-72.

Conclusions

The record in this proceeding establishes[39/] that respondent Germaise, who represented the issuer in the Regulation A offering, and respondent Quinn, who represented the underwriter in the offering, failed to disclose in the notification and offering circular the material fact that they were partners in the practice of law from mid-November 1968, and that they failed to advise the underwriter of that fact. By these omissions respondents misled investors and potential investors in contravention of the antifraud provisions of the federal securities laws, misled the Commission, and violated Canon 6 of the Canons of Ethics of the American Bar Association by representing clients with conflicting interests without first obtaining their express consent after a full disclosure of the facts.

The record further establishes that respondents, in part knowingly and in part through failure properly to carry out their professional responsibilities as attorneys, were responsible for the failure of the Bagels offering circular to disclose, as required, a number of material facts, i.e. $35,000 in loans to be repaid out of the proceeds of the offering, $30,000 in short-term loans made to the company by directors and promoters, and a contract to purchase real property for $60,000 (as well as a recent purchase of equipment on the premises for $10,000). In addition, respondents permitted the offering circular to misrepresent material facts concerning the number and identity of the shareholders

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39/ The findings and conclusions reached herein are based upon clear and convincing evidence even though the applicable standard of proof is the lesser one of the preponderance of the evidence. In the Matter of Murray A. Kivitz, Securities Act Release No. 5163, June 29, 1971.

of the ten corporations acquired by Bagels.

As respects respondent Quinn, the record further shows his conviction on July 31, 1970, by a United States District Court, confirmed by the U.S. Court of Appeals, of violations of the registration and antifraud provisions of the Securities Act of 1933.

It is concluded that the foregoing findings of misconduct by the respondent establish proof, as charged in the order, of unethical and improper professional conduct and a lack of character and integrity within the meaning of those terms as used in Rule 2(e) of the Commission's Rules of Practice (17 CFR 201.2(e)).

RESPONDENTS' CONTENTIONS

Respondents make a number of contentions alleging denial of due process and urge that it would be improper or inappropriate to impose on them any disciplinary action predicated upon the charges in this proceeding. As concluded below, there is no merit to any of the charges of lack of due process.[40/]

Respondents contend that they sustained hardship and prejudice from the fact that the hearing was held in Washington, D.C. rather than in New York, New York, where they practice. The hearing, which commenced on January 25, 1971, had been scheduled to begin on that date in Washington by order dated November 25, 1970, two months before the

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40/ In seeking to characterize one of the arguments of the Office of General Counsel with the Shakespearian phrase "sound and fury, signifying nothing" (Macbeth to Seyton, Act V), respondents call to mind a phrase that aptly describes their unfounded claims of lack of due process.

scheduled hearing date. Yet it was not until Thursday, January 21, 1971, that respondents requested a change of venue; this was denied primarily upon the ground of lack of timeliness. By the time respondents made their request witnesses were already under subpoena to appear in Washington and the Office of General Counsel had understandably made its plans based upon the hearing being in Washington. Respondents contend they were prejudiced by a lack of access to their office and their records. This contention lacks validity for a number of reasons. To begin with, the issues in the proceeding are clearly spelled out in the order for proceeding and respondents could easily have brought with them whatever business records they regarded as necessary to their defenses — or they could have had personnel from their law firm 41/ bring to Washington whatever records were required even after the hearing commenced. Significantly, although respondents during the course of the hearing renewed their request for a change of venue, they never requested a continuance for the specific purpose of enabling them to produce relevant records. 42/ Moreover, the essential facts upon which the findings herein are predicated are essentially uncontroverted and there is no indication that recourse to the firm's records would

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41/ The letterhead respondents were using in January 1971 listed seven attorneys besides the respondents; presumably the firm had appropriate clerical and stenographic support. In addition, respondents' letterhead indicates an "Of Counsel" in Washington, D.C., whose office was presumably available to respondents.

42/ The only request for continuance by Germaise for the purpose of obtaining records related to a check for $3,000 covering the initial payment on his $7,500 fee from Bagels. The need for this was obviated when it was conceeded that this check was paid to Germaise personally before the partnership commenced and that proceeds of the check went to him, not the partnership.

materially alter them. Respondents have sustained no prejudice.

Secondly, respondents contend that evidence concerning their representation of clients in another, unrelated offering, the Taco-Si offering, which was offered and received for the limited purpose of showing respondents' state of mind in connection with the charges in this proceeding, was improperly received. The short answer to this contention is that in arriving at the findings and conclusions in this proceeding no reliance has been placed, directly or indirectly, on any testimony or exhibits relating to the Taco-Si matter.

Respondents also profess to be surprised by the contention of the Office of General Counsel in its brief that the respondents' failure to advise the underwriter of their law partnership violated Canon 6 of the Canons of Professional Ethics of the ABA. This contention is without merit since the order for proceeding specifically alleged respondents' failure to disclose their partnership to the underwriter and also characterized such failure as "unethical and improper professional conduct" within the meaning of the Commission's Rule 2(e). Respondents were thus "sufficiently informed of the nature of the charges" against them.[43/]

Respondent Germaise contends that when he testified at the New York Regional Office of the Commission on July 30, 1969, in the course of the Bagels investigation, he produced certain of his files and papers relevant to the Bagels offering pursuant to subpoena that were never returned to him, and he contends that the non-availability of these papers to him has prejudiced his defense. The Office of General Counsel

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43/ General Aeromation, Inc., 40 SEC 21, 22-23 (1960).

contends, and produced a Commission attorney present at Germaise's examination to so testify, that all of Germaise's files and papers (other than those introduced as exhibits, and which are not here in issue) were returned to Germaise at the time he completed his testimony.[44/]

Germaise first made a demand for the papers at the time of this hearing even though some 18 months had elapsed since the time of his investigative testimony and over 4½ months had elapsed since this proceeding had been instituted. Taking this into account, together with the demeanor of the witnesses who testified on the question and the record as a whole, it is concluded that the materials Germaise produced were in fact returned to him when he completed his investigative testimony.[45/]

Moreover, the work papers allegedly not returned to Germaise related to his preparation of the offering circular and related papers for the Bagels offering. As such they would have shed little if any light on the facts involved in the principal findings made herein, e.g. when the partnership was formed, the failure to give notice thereof, the failure of the offering circular to make certain disclosures, etc. Germaise himself was rather vague about what he hoped to establish through the allegedly unreturned papers,[46/] during the course of the hearing and his speculation at p. 69 of respondents' brief about what such papers might show indicates that his "proof" would relate to matters that are not really issues in this proceeding. (The question is not what aspects

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44/ The transcript of his testimony contains no indication whether the files and papers were returned to Germaise or not.

45/ Germaise's contrary testimony is not credited.

46/ R. 133-134, 154, 549-551.

of due diligence Germaise carried out satisfactorily but whether there are some aspects of due diligence in which he failed).

Respondents contend also that they were denied due process because of an alleged failure by the Office of General Counsel to produce materials under Rule 11.1 of the Commission's Rules of Practice (17 CFR 201.11.1) which applies administratively the Jencks Act provisions of 18 U.S.C. 3500. There is no merit to this contention. Various notes taken by Commission attorneys were produced for in camera examination by the hearing examiner and were found not to constitute "substantially verbatim" transcripts of the witness's oral statements.

Lastly, respondents contend that the Office of General Counsel should have produced for their examination transcripts of Glantz's testimony before the Attorney General of the State of New York. The Office of General Counsel represented that it had no such transcripts in its possession and had never seen any. A federal agency has no obligation under the Jencks Act to produce material in the possession of state authorities.[47/]

DISCIPLINE REQUIRED IN THE PUBLIC INTEREST

The charges made and established in this proceeding are of a most serious nature. The role of attorneys in the disclosure process provided for in the Securities Act of 1933 is critical to the purposes

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47/ Beavers v. U.S., 351 F.2d 507, 509 (C.A. 9, 1965).

of the Act. Since the Commission under the statutory scheme does not approve or pass upon the accuracy of the various statements and reports filed with it, it is particularly important that attorneys who prepare and verify these materials, such as the notification and offering circular involved in this proceeding, assume the obligation and responsibility of diligently verifying the accuracy and completeness of such documents. The Commission has by the promulgation of Rule 2(e) of its Rules of Practice established a means for disqualifying attorneys who have proved themselves unable or unwilling to carry out such responsibilities.[48/]

A sanction in a lawyer's disciplinary proceeding must be just to the public and must be designed to correct any anti-social tendency on the part of the attorney, as well as to deter others who might tend to engage in like violations; it must be fair to the attorney but the duty of the disciplining authority to society is paramount.[49/]

Unfortunately the picture that is painted by this record is one in which respondents, both well-experienced in securities laws, defaulted in the performance of their important functions — whether because they became too closely personally involved with the issuer or for whatever reason — and in part knowingly and in part carelessly allowed the notification and offering circular to contain materially false and misleading information and to fail to disclose information that should have been disclosed.

48/ Disbarment is designed to protect the public. In re Ruffalo, 390 U.S. 544, 550 (1968).

49/ State ex rel Florida Bar v. Murrell, 74 So. 2d 221, 227 (S. Ct. Fla. en banc, 1954).

Taking into account all mitigating factors urged, including the absence of prior disciplinary proceedings against respondents, it is concluded that a 2-year suspension of eligibility to practice would adequately and appropriately serve the public interest insofar as the unethical and unprofessional conduct respecting the Bagels offering is concerned. As to respondent Quinn, however, there must be considered additionally his criminal conviction of violating the registration and antifraud provisions of the Securities Act.

That his conviction arises out of events that occurred some times ago, in 1962 and 1963, does little to blunt its importance in light of the subsequent unethical conduct found in this proceeding. Quinn has not mended his ways. Moreover, as already noted, the Court of Appeals decision sustaining his conviction found that Quinn was not just peripherally involved but was the "moving spirit" in the brokerage firm that served as the vehicle for the fraudulent sales of stock there found. The gravity with which any conviction of an attorney of a felony or of a misdemeanor involving moral turpitude is viewed by the Commission is reflected by its recent amendment to Rule 2(e) providing for automatic disqualification in such event.[50/] While this amendment is not applicable to Quinn since it was issued subsequent to the institution of this proceeding, it is concluded that Quinn's felony conviction, coupled with his unethical and improper professional conduct in connection with the Bagles offering, requires that he be permanently

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50/ 17 CFR 201.2(e)(2).

disqualified from practice before the Commission.[51/] Accordingly,

IT IS ORDERED that Irwin L. Germaise be, and he hereby is, denied the privilege of appearing or practicing before the Commission for a period of two years from the effective date of this order, and

IT IS FURTHER ORDERED that Thomas F. Quinn be, and he hereby is, permanently disqualified from appearing or practicing before the Commission: Provided, however, that if the conviction of Thomas F. Quinn mentioned herein should be reviewed and reversed on all counts his disqualification shall, upon application, be reduced to a period of two years from the effective date of this order.

This order shall become effective in accordance with and subject to the provisions of Rule 17(f) of the Commission's Rules of Practice (17 CFR 201.17(b)).

Pursuant to Rule 17(f), this initial decision shall become the final decision of the Commission as to each party who has not, within fifteen (15) days after service of this initial decision upon him, filed a petition for review of this initial decision pursuant to Rule 17(b), unless the Commission, pursuant to Rule 17(c) determines on its own initiative to review this initial decision as to him. If a party timely files a petition for review, or the Commission takes action to

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51/ It is well established in the courts that conviction of a felony or other crime involving moral turpitude is ground for disbarment. In the Matter of Paul M. Kaufman, Securities Exchange Act Release No. 8925, July 2, 1970, p. 3, and cases there cited. The possibility that certiorari may be sought and obtained to review Quinn's conviction does not preclude his immediate disqualification from practice subject to removal of the disqualification, upon application, in the event that any review that may be granted results in a reversal of his conviction on all counts. See In re Matter of Paul M. Kaufman, cited above.

review as to a party, the initial decision shall not become final with respect to that party. 52/

David J. Markun
Hearing Examiner

October 29, 1971
Washington, D.C.

52/ To the extent that the proposed findings and conclusions submitted by the parties are in accordance with the views herein they are accepted, and to the extent they are inconsistent therewith they are rejected. Certain proposed findings and conclusions have been omitted as not relevant or as not necessary to a proper determination of the issues presented.