BEFORE THE SECURITIES COMMISSIONER

OF THE STATE OF DELAWARE

IN THE MATTER OF:	)	
	)	
HIBBARD, BROWN & CO., INC.,	)	
MICHAEL MARTONE,	)	Case Nos. 90-01-02, 90-07-04,
BRENDAN D. HART, and	)	and 91-03-04
JOHN B. MURPHY,	)	
	)	
Respondents.	)	

W. Michael Tupman, Deputy Attorney General, Department of Justice Wilmington, Delaware, attorney for the State.

Joseph A. Rosenthal, Esquire, Rosenthal, Monhait & Gross, P.A., Wilmington, Delaware;
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attorneys for the respondents.

OPINION

February 13, 1992
Wilmington, Delaware

Charges were issued by the Delaware Securities Division on June 19, 1991, against the respondents, Hibbard Brown & Company, Inc., ("Hibbard Brown"), a broker-dealer registered to sell securities in Delaware, and Michael Martone ("Martone"), Brendan D. Hart ("Hart"), and John B. Murphy ("Murphy"), agents of Hibbard Brown. Martone and Hart were registered to sell securities in Delaware at the time of their alleged violations, but Mr. Murphy was not registered at the time of his alleged violation.

The notice of allegations ("Notice") charged the following violations:

(1) violations of 6 Del. C. sections 7303(2) and 7316(a)(2) by Hibbard Brown and Martone in the sale of securities to , a Delaware resident--the violations consisting of willful misrepresentations and omissions of material facts concerning the securities;

(2) violations of 6 Del. C. sections 7316(a)(7) and 7316(a)(2) by Hibbard Brown and Martone in the sale of securities to --the violations consisting of dishonest and unethical conduct because of respondents' failure to conduct a "due diligence" review of the securities prior to recommending them and because there was no reasonable basis for believing the securities were suitable for the investor;

(3) violations of 6 Del. C. section 7316(a)(10) by Hibbard Brown in connection with its sales of securities to

because it failed to supervise reasonably its agent Michael Martone;

(4) violations of 6 Del. C. sections 7303(2) and 7316(a)(2) by Hibbard Brown and Hart in the sale of securities to , a Delaware resident--the violations consisting of willful misrepresentations and omissions of material facts concerning the securities;

(5) violations of 6 Del. C. sections 7316(a)(7) and 7316(a)(2) by Hibbard Brown and Hart in the sale of securities to --the violations consisting of dishonest and unethical conduct because of respondents' failure to conduct a "due diligence" review of the securities prior to recommending them and because there was no reasonable basis for believing the securities were suitable for the investor;

(6) violations of 6 Del. C. section 7316(a)(10) by Hibbard Brown in connection with its sales of securities to because it failed to supervise reasonably its agent Brendan Hart;

(7) one violation by Hibbard Brown and Murphy of 6 Del. C. section 7314 in connection with the offer of a security to , a Delaware resident--the violation consisting of Murphy's failure to register to sell securities in Delaware as an agent of Hibbard Brown; and

(8) one violation of 6 Del. C. section 7316(a)(10) by Hibbard Brown in connection with its offer of a security to because it failed to supervise reasonably its agent John B. Murphy.

The Notice also included allegations that the securities offered or sold to the Delaware residents were not registered or exempt from registration, as required by 6 Del. C. section 7304, but those charges were withdrawn at the hearing.

The securities purchased by included interests in the following companies: Children's Creative Workshop, Ltd.; DreamCar Holdings, Inc.; Truvel Corporation; and Asset Growth Partners, Inc. These securities were purchased during the period of September 1989 through December 1989. The Notice alleged that lost $15,312 as a result of these investments through Hibbard Brown.

The securities purchased by included interests in the following companies: Trans-Atlantic Video, Inc.; Fireplace Manufacturers, Inc.; Children's Creative Workshop, Ltd.; F.A. Computer Technologies, Inc.; News Communication, Inc.; and Graystone Companies, Inc. These securities were purchased during the period of August 1989 through January 1990. The Notice alleged that lost $39,389 as a result of these investments through Hibbard Brown.

The respondents requested a hearing, which was held during the period of October 28 through November 8, 1991, including a hiatus of five days. The State presented the testimony of the

two Delaware investors and their spouses, plus the testimony of , the Delaware resident who was allegedly solicited by Hibbard Brown, and Leon Minka, a securities analyst for the Delaware Securities Division. Additionally, the State introduced into the record 130 exhibits that included registration records, prospectuses, Hibbard Brown research reports, and financial reports of the issuers of the securities that were sold. The State's exhibits also included several cassette tapes and a transcript of the tapes, containing post-sale telephone conversations between and several Hibbard Brown agents.

I. SUMMARY OF THE TESTIMONY

A. The State's Case

Mr. Minka, the State's securities analyst, testified as to various financial problems or characteristics of the securities he observed in the registration statements, prospectuses, and financial reports of the issuers. (Transcript at 1-36 to 1-153).[1] During his lengthy cross examination, the respondents established that Mr. Minka had little personal knowledge as to the basis for many of the allegations in the Notice. (Tr. at 1-154 to 2-114).

testified that he worked as a pipe-fitter at the DuPont Experimental Station, with annual earnings of

[1]References to the transcript are hereinafter abbreviated to "Tr." References to State's exhibits will appear as "S-1" et seq., and references to the respondents' exhibits will appear as "R-1" et seq.

approximately $33,000 or $34,000 in 1989 at the time of his purchases. (Tr. at 2-123, 124). He was a high school graduate with no prior investment experience other than purchasing DuPont Company stock through the company's thrift plan. (Tr. at 2-125, 3-49). He was solicited in the autumn of 1989 at his place of work by a telephone call from Michael Martone, who asked if he wanted to invest in stocks. Although said "no," Martone called him back several times and finally talked into purchasing stocks through Hibbard Brown. (Tr. at 2-126, 127). The first security purchased was Children's Creative Workshop, Ltd. ("Children's Creative"), on or about September 19, 1989. (Tr. at 2-130). Martone recommended the security, telling that "it was a good company coming up and there were a lot of good things happening within the company that he couldn't tell me at that time." (Tr. at 2-130). Martone said many times "there's no downside risk" to the investment, but he did not otherwise discuss risks. (Tr. at 2-131). Although at the time did not understand the terms "bid" and "asked," Martone did not explain them. Martone did tell that the security was about to be listed on NASDAQ,[2] which found

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[2]"NASDAQ" refers to the National Association of Securities Dealers Automated Quotations system, the electronic over-the-counter market whereby securities firms display their bid and asked prices for certain securities in which they make a market. NASDAQ-listed securities are listed in financial newspapers whereas "pink sheet" securities (securities listed in inter-dealer trading sheets that are printed on a daily basis by National Quotation Bureau, Inc.) are not.

significant because he wanted to be able to follow the price movements of the security. (Tr. at 2-132).

Mr. subsequently bought additional shares of Children's Creative at the urging of Martone, who repeatedly called and told him that he needed to increase the number of his shares "into a round lot." (Tr. at 2-133). Again Martone told there was "either no downside risk or very little downside risk." (Tr. at 2-133). Although Martone recalled receiving some financial information about the security, it was not received until January 1990 or thereabouts, well after the sale.

next investment, in or about November 1989, was in a company named DreamCar Holdings, Inc. Martone recommended this stock, telling it was a "a hot company" that "was going to do things." (Tr. at 2-134). Again Martone disclosed no risks, and he did not explain the bid and asked pricing structure of the security. was told that "big things are happening and they are about ready to start producing cars." (Tr. at 2-135).

In December 1989 bought stock in Truvel Corporation upon Martone's recommendation. No risks were disclosed and no financial statements or other data were provided. (Tr. at 2-136, 137). Ten days after the purchase of Truvel, Martone called again and recommended that sell the stock, telling him it was "time to get out" but providing no reason. (Tr. at 2-137, 138). Instead of a cash payment, however, Martone recommended

that use the proceeds of the sale to buy Asset Growth Partners ("Asset Growth"). Again no risks were discussed. (2-138, 139). Martone urged to buy Asset Growth because "it was the next hot stock" and because Martone had made money for on Truvel. (Tr. at 2-139).

Prior to his investment purchases, had discussed his investment objectives with Martone. He told Martone that he was looking for "long-term growth," a rate of return higher than the rate that certificates of deposit were then paying. However, did not say that his objective was speculation. (Tr. at 2-143). Rather, he made it clear to Martone that he could not afford to risk his investment principal. (Tr. at 3-31). The lump sum of money he used for these investments consisted of the proceeds of the sale of his personal residence. (Tr. at 3-36).

also testified that, in late December of 1989, he bought a book on investing and participated in a computer "bulletin board club" in which members discussed their investments. (Tr. at 2-146, 2-147, 3-34).

In January 1990 through March 1990 recorded his telephone conversations with agents of Hibbard Brown on two cassette tapes. (Tr. at 3-23). The revised transcript of these tapes, State's Exhibit 103, purportedly shows the chronology of the conversations. testified that the initial transcript had reversed the two sides of Tape 2, which is State's Exhibit 102-B. (Tr. at 3-24). I am uncertain that even the

revised transcript presents the conversations in accurate chronological order.

The State's next witness was , a Delaware resident who also was employed by the DuPont Company at the time he purchased investments through Hibbard Brown. had a master's degree in chemistry and had been employed mostly as a chemist. (Tr. at 3-157, 158). At the time of his investments he had a sales position in the area of chemicals. (Tr. at 3-112). At that time his annual income was approximately $60,000, his wife's was about the same, and their net worth was approximately $250,000. (Tr. at 3-181). had limited investment experience, having been given DuPont stock as employment bonuses, having once bought $1400 worth of stock in a DuPont competitor, having once bought an interest in an unsuccessful real estate limited partnership sold to him by his boss, and having invested in some mutual funds. (Tr. at 3-113, 170).

testified that he was solicited on the telephone by Brendan Hart during the summer of 1989. Mr. Hart asked if he were interested in investing in the stock market, and said that he might be. Three or four weeks later Hart met at his Delaware home. Hart asked how much money he had to invest in stocks, and said $5,000 or $10,000. At this meeting told Hart that he ( ) knew nothing about the stock market and was looking for good advice. also mentioned that he was concerned about losing his job with DuPont.

(Tr. at 3-115, 121). Hart said that he could provide good advice. (Tr. at 3-116).

Asked about investment objectives, Mr. explained that he had two: one short-term and one long-term. His short-term objective was to survive the threat of losing his job, and his long-term objective was to retire in eight or nine years at age 58. (Tr. at 3-120). Although I think these are really employment objectives rather than investment objectives, whatever they were Mr. explained them to Mr. Hart. (Tr. at 3-120, 121). Asked to be more precise about his investment objectives, testified that he was looking for "[s]ome small growth or some small loss, because if I didn't have a job I might need that money to live on for a while." (Tr. at 3-121). He testified that he was concerned about the liquidity of his investments because if he did not have a job he would need the money for house payments. told Hart that was concerned about "tying up my money," and Hart said not to worry because once decided to sell a security he would receive a check in a few days. (Tr. at 3-122).

On cross examination, testified that he did not recall telling Hart that one of investment objectives was speculation. (Tr. at 3-187). When counsel pressed him to concede that it was possible, in view of the lapse of time since their conversation, that had said speculation was one of his objectives, said that it was possible but to his mind

speculation was anything other than an insured investment. (Tr. at 3-188).

The first security Hart recommended to was stock in a company named "Trans-Atlantic Video, Inc." (hereinafter "Trans-Atlantic"). The recommendation came in a telephone call from Hart to that followed their meeting, and Hart said the stock was a "good buy." (Tr. at 3-116). Hart said that Trans-Atlantic had "rights to movies like Dick Tracy." (Tr. at 3-117). No risks were mentioned by Hart, and there was no explanation of the bid and asked pricing structure of the security. (Tr. at 3-118).

After purchase of Trans-Atlantic, Hart called again to advise that he needed to buy additional stock because he "needed to diversify." (Tr. at 3-122). On Hart's recommendation, then purchased shares of Fireplace Manufacturers, Inc. Hart said it was a good investment because a lot of people burn wood these days. No risks of the investment were discussed. (Tr. at 3-123).

Mr. next purchase was on September 20, 1989, when he purchased shares of Children's Creative Workshop, Ltd. Mr. Hart had called him to recommend Children's Creative, saying that he had been in a meeting with a research group or with his management. (Tr. at 3-125). Mr. was unable to recall Hart's description of the Children's Creative business. Hart did not send any financial information about the company. (Tr. at 3-125). Five days after this purchase, Hart called

again and recommended that buy more shares of Children's Creative. No risks were discussed, but bought more shares. At this time sold his shares of Trans-Atlantic and applied the proceeds to his purchase of Children's Creative. (Tr. at 3-125), 126). On October 17, 1989, bought still more shares of Children's Creative after receiving a telephone call from Hart recommending the additional purchase. Again, no financial documents were provided and no risks were discussed. (Tr. at 3-127).

On November 8, 1989, Mr. Hart called to recommend another stock, F.A. Computer Technologies, Inc. ("FACO"). This time argued with Hart because had some personal knowledge of the computer industry and knew that there was "cutthroat" competition. (Tr. at 3-128). Hart's response was that the research group of Hibbard Brown had researched the stock and highly recommended it. There was no mention of risks or the bid and asked pricing structure of securities. (Tr. at 3-128). The purchase of FACO was made in part from the proceeds of a sale by of stock in Fireplace Manufacturers.

On December 19, 1989, Hart called again to recommend the purchase of stock in Truvel Corporation, which bought. could remember nothing about the company at the hearing, but he did not think there was any discussion of risk by Mr. Hart. Ten days after this purchase of Truvel, Hart called again to recommend that sell those shares and buy shares in a different company. followed the advice and purchased

shares in News Communications, Inc. There was no discussion of risk or the difference between the bid and asked prices. (Tr. at 3-129 to 3-131).

On January 17, 1990, purchased shares of Graystone Companies, Inc., on Hart's recommendation. Hart did not mention risk. (Tr. at 3-132). On March 5, 1990, sold his shares of Graystone to buy shares of Trans-Atlantic Video. Hart recommended the transactions, saying that had made money on Trans-Atlantic in the past. Hart said he thought the Trans-Atlantic stock would become worth a lot more than its then-current price of two dollars. No risks were discussed. (Tr. at 3-133). Slightly more than two weeks later, Hart called again to recommend that purchase more Trans-Atlantic stock.

followed Hart's advice. testified that Hart said "this stock was really going to take off." (Tr. at 3-133, 134).

Subsequent to March 1990 purchase, Hart continued to call to recommend that he buy more stock. Hart was persistent to the point where had to hang up on him. (Tr. at 3-140).

On July 16, 1990, called Hart to inquire about the prices of the securities had bought. wrote the values on a piece of paper that was introduced into the hearing record as State's Exhibit S-104. calculated from these figures that he had lost approximately $5,000 altogether. Three days later, on July 19, 1990, called Hart to sell the securities. This time Hart gave very different numbers for two

of the securities, with the result that had lost $22,000. (Tr. at 3-141, 142). then wrote a letter of complaint to the president of the firm, Richard Brown. (Tr. at 3-143).

Also about this time, Mr. spoke with a representative of the brokerage firm Janney, Montgomery Scott ("Janney"). attempted to sell his securities through Janney, but the representative told him, "We don't handle stuff like this." (Tr. at 3-216). was told that only four or five firms would deal in those securities, and none was local. also spoke with an employee of the Delaware Department of Justice, who led to believe that he could sell his securities only through Hibbard Brown. (Tr. at 3-216, 217).[3]

The spouses of and also testified. testified that at the time of the purchases in 1989 she was employed as a supervisor at A.I.G. Marketing, earning approximately $24,999 annually. She had no accounts or investments other than $600 in savings and some stock in her employer's company stock participation plan. She was a high school graduate. She could recall very little of the financial transactions at issue. (Tr. at 3-14 to 3-16).

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[3]After the issuance of this opinion, I intend to inquire as to the employee who allegedly told Mr. that Hibbard Brown controlled the market and, if appropriate, reprimand that individual. Investigators have no business making unproven allegations about a brokerage firm to members of the public. I note, however, that at this time there were several inexperienced investigators who had been recently hired by the Securities Division.

testified that she was employed by ICI as a medical writer, earning approximately $52,000 in 1989. She and her husband had some investments, including a $60,000 certificate of deposit. She had a B.S. degree from the University of Delaware in medical technology. She recalled that her husband had dealings with Brendan Hart and that Hart placed a telephone call to her on or about March 29, 1990 at her place of work. Her husband had told Hart that he would not invest any more money with him, and she believed that Hart had called her because he would not take "no" for an answer. She testified that it was impossible for them to invest more money at this time because her husband's department at DuPont was being dissolved, and he would have to find a position with another company or retire. She recalled Hart asking that they invest another $10,000 into either Children's Creative Workshop or Trans-Atlantic Video. Mrs. testified that Hart did not want her to say "no" during their conversation, and she characterized him as "very aggressive and what I call pushy salesperson." (Tr. at 3-3 to 3-9).

The State's final witness was , a Delaware resident who testified that he received a telephone call from John B. Murphy in March 1991. Murphy identified himself as an agent of Hibbard Brown and offered to sell shares of stock in a company named "K.B. Communications." testified that Murphy told him that Murphy had a "special private trading block" of the stock that was trading at $5 3/8 per share but that Murphy would sell it to him for $5 per share. During

this call Murphy told that "the head of MCA was meeting with the head of some other major record producer and they were going to control 90 percent of the European and Asian market." (Tr. at 4-3, 4, 17). A week later Murphy called again and told him that the stock was then trading at $7 3/8 per share and that should have bought it when he had the opportunity. Murphy berated for not buying the stock and then hung up abruptly. called back, and Murphy said, "I don't have time to mess with people that don't have the balls to put in the money that it takes to make a transaction like this go." (Tr. at 4-14, 21). On either this occasion or the prior call, said his office was in West Palm Beach, Florida. (Tr. at 4-6). declined to buy any stock from Murphy, however. (Tr. at 4-5).

B. The Respondents' Case

The respondents presented their case through the testimony of Hibbard Brown officials and employees: Richard B. Brown, the president; William Howard, the branch manager of the Red Bank, New Jersey office where Martone and Hart worked; John Attalienti, the director of research; B. DeJuan Stroud, the director of compliance; and Michael Martone, Brendan Hart, and John B. Murphy, the sales agents of Hibbard Brown. The respondents also introduced a large number of documents into the record, including their research files on securities, weekly research notes, and regulatory compliance and procedures manuals.

Mr. Brown testified that he and Peter Hibbard formed Hibbard Brown in 1986 in Greenbelt, Maryland. (Tr. at 4-77). The "thrust" of the firm was initially in financial planning, but that focus was changed due to tax law changes. (Tr. at 4-80). After the stock market drop in October 1987, Mr. Brown decided to focus the business at the retail level, and he opened an office in New York. (Tr. at 4-81). In July or August 1988 he purchased some offices from Sherwood Industries ("Sherwood") and closed his other offices. (Tr. at 4-81, 82). At the time of the hearing, Hibbard Brown employed approximately 650 individuals at 14 branch offices. Prior to the purchase of the Sherwood offices, his firm employed approximately 150 individuals. (Tr. at 4-82). Mr. Hibbard terminated his relationship with Hibbard Brown at the time of the purchase of the Sherwood offices. (Tr. 4-83).

Mr. Brown testified that Hibbard Brown is a "full service" brokerage firm with 79,000 customers. (Tr. at 4-83, 84). The firm is a member of the Boston Stock Exchange and Philadelphia Stock Exchange and clears its own transactions. (Tr. at 4-84 to 4-86). The firm does not allow discretionary accounts or margin accounts. (Tr. at 4-87). The firm has never had a customer complaint of churning. (Tr. 4-87). Although the firm has had some customer complaints from time to time, only 35 have resulted in litigation. (Tr. at 4-87, 88). The firm does not deal in penny stocks, though it did prior to January 1, 1990. (Tr. at 4-87, 88). When it did deal in penny stocks, Hibbard Brown never

encouraged its sales force to unload them out of its inventory. (Tr. at 4-89).

Mr. William Howard testified that he is a high school graduate and the branch manager of Hibbard Brown's Red Bank, New Jersey office. (Tr. at 4-90, 4-91). The office has approximately 70 employees. (Tr. at 4-92). Throughout the office Mr. Howard has assistant managers who operate as his "eyes and ears" to keep him informed as to what takes place around the office on a daily basis. (Tr. at 4-93).

Mr. Howard testified that he opens all the mail that comes into the office on a daily basis to ensure that he reviews all customer communications to registered representatives so that he can spot potential problems and handle them quickly. (Tr. at 4-94, 95). After opening all the mail, Mr. Howard then reviews all firm-generated confirmation slips for transactions of the previous day. He reviews the confirmation slips to ensure "blue sky qualification." (Tr. at 4-96). After reviewing all the confirmation slips, he then reviews and signs off on all order tickets for that day's trading. (Tr. at 4-97). He compares each order ticket to the new account report for the customer and to the customer's stock page. (Tr. at 4-98). He checks each new account report to ensure the report is filled out correctly in its entirety, and he signs off on the new account report as well as on the order ticket for each trade. (Tr. at 4-98, 99). The firm depends on the new account form to determine suitability of the security for the customer. (Tr. at 4-100).

Mr. Howard testified that although Hibbard Brown is a full service brokerage, its "main forte in equities has been in emerging growth companies." (Tr. at 4-10). The firm trains its representatives "to gather as much information as a client is willing to give them in terms of what their investment objectives are." (Tr. at 4-101). He acknowledged that the emerging growth companies area is a "higher risk area of the marketplace and certainly is not an area that's suitable for every investor." (Tr. at 4-10).

Mr. Howard testified that the procedures and functions of the branch office manager are stated in a Hibbard Brown procedures manual, with which he is familiar. (Tr. at 4-93). The procedures and functions stated in the manual are followed every day. (Tr. at 4-103). Item number 11 of the general outline for branch managers specifies that the manager is to "[i]nsure all registered representatives are properly qualifying and making suitable recommendations." (Tr. at 4-104).

Mr. Howard testified that Hibbard Brown is continually training its representatives on an ongoing basis. (Tr. at 4-105). At least one or two meetings are held each week where customer suitability is emphasized and updates on particular companies are provided. (Tr. at 4-105, 106). During the market update in such calls, Mr. Attalienti would provide recommendations in three or four listed securities and three to six over-the-counter securities, besides highlighting a mutual fund. (Tr. at 4-108). The research department would forward

current 10-K annual reports or 10-Q quarterly reports on companies in which the firm is making a recommendation. (Tr. at 4-108).

Registered representatives at Hibbard Brown are trained that if there is a customer problem, it is to be brought to the attention of the branch manager immediately. Mr. Howard would then contact the customer and try to resolve the problem on the branch level. If he were unable to do so, he would forward the matter to the compliance department. (Tr. at 4-11).

Mr. Howard first became aware of complaint when he saw a letter of complaint had written to the National Association of Securities Dealers ("NASD"), an industry self-regulatory organization. Howard then called to see if Howard could be of any help. (Tr. at 4-111, 112). Howard first became aware of complaint in June 1990. He called and offered his services to try to resolve the problem. (Tr. at 4-112).

Mr. Howard testified that Hibbard Brown's "whole philosophy towards the market is that diversification is key." (Tr. at 4-113). In the firm's opinion, "all stocks have risks." (Tr. at 4-113). Representatives are trained to encourage diversification, having the customer invest in a number of companies. (Tr. 4-114).

On cross examination, Mr. Howard acknowledged that although the new account form is important to the suitability determination, Hibbard Brown does not require that the customer

see the completed form or sign it. (Tr. at 4-123). He stated that although the procedures manual stresses that the firm is in a higher risk area of the market and that extreme care must be taken for the representative to know the customer, the only two questions on the form that pertain to financial capabilities are one about income and one about net worth. (Tr. at 4-130). He also testified that his branch office regularly receives 10-K and 10-Q financial reports as they are disseminated. (Tr. at 4-132, 133). He stated that "diversification" may include either different types of investments or different stocks, depending on the customer's wishes. (Tr. at 4-137, 138). On redirect examination, Mr. Howard stated that Hibbard Brown's determination of customer suitability "really can't be overstated" and that "[i]t's an ongoing process." (Tr. at 4-155).

John D. Attalienti testified that he is the director of research at Hibbard Brown. (Tr. at 5-4). He testified that he "follows" about 100 securities at a time, 40% of which are over-the-counter. (Tr. at 5-20). He and his staff review companies that come to their attention, about 75 to 80% of which are "weeded out." (Tr. at 5-23). They utilize an "extensive network of computers and data bases." (Tr. at 5-23). They review industry trends and do "screening" relative to the "dynamics that are at work for these particular companies that come to our attention." (Tr. at 5-23). They look at how other stocks in the industry have performed, talk to management about its plans, and take field trips to see the companies if that is

possible. (Tr. at 5-23, 24). The most important element in dealing with the small company is the quality of the management. (Tr. at 5-24). After a decision to recommend a security is made, the information is disseminated through the Hibbard Brown Weekly Research Notes which are the "flagship publication" of the firm. (Tr. at 5-25). Additionally, the firm sometimes issues individual company reports that vary from four to 12 pages. There are also conference calls to all the branch offices. (Tr. at 5-25). All financial reports on recommended companies are automatically sent to the branch offices. (Tr. at 5-26).

In analyzing a particular company, Mr. Attalienti first looks at its business plan or goals. He then analyzes the available financial reports and talks to management. He may also go to trade shows, talk to customers of the company, and talk to others on Wall Street about the company. (Tr. at 5-26, 27). He also relies on his data base and "feel for what's happening in the stock market." (Tr. at 5-28). This is called a "top-down approach to research." (Tr. at 5-28). He noted that since late 1989 Hibbard Brown had been "aggressively telling people that small capitalization stocks would be the place that would outperform other segments of the market," and indeed at the end of 1991 that had been the case. (Tr. at 5-28, 29). He defined "small capitalization" companies as those having a market capitalization of 250 million dollars and under. (Tr. at 5-13).

Of the securities recommended to the Delaware investors, two were what Mr. Attalienti called "concept companies." These are

companies without an established track record, particularly in the financial area, but they have a concept, an idea, or a business plan. (Tr. at 5-31). Children's Creative and DreamCar were concept companies. Children's Creative was pursuing a niche in the speciality retailing industry based on its belief that the birth rate was increasing. (Tr. at 5-31, 32). They wanted to avoid the mass merchandising technique of Toys-R-Us. (Tr. at 5-32). In fact, the idea of Children's Creative competing with Toys-R-Us was "absolutely absurd." (Tr. at 5-46).

Bernard Tessler was the founder of Children's Creative, and he had previously operated a concept company called "The Enchanted Village." He presented a 50-page business plan to Hibbard Brown. (Tr. at 5-34). Philip Baird was also involved in the management of Children's Creative, and he impressed Mr. Attalienti because Baird "was in at the very beginning of The Gap," a successful retail chain. Another important manager was Sidney Stein, who had been associated with Waldenbooks. (Tr. at 5-35).

Although Mr. Tessler's company "The Enchanted Village" had filed for bankruptcy and was liquidated, he had learned some lessons from that experience. The biggest lesson was not to locate stores near malls. (Tr. at 5-37). Mr. Attalienti did not consider The Enchanted Village to be a failed venture because "[t]he company had gotten some very good press and the idea was generally well accepted." (Tr. at 5-38).

DreamCar was the second concept company recommended by Hibbard Brown. This company intended to "remanufacture" the so-called "muscle cars" of the late 1950s and 1960s. The company would find shells of these old cars and add new transmissions, brake systems, stereo systems, air conditioning, and other such improvements. (Tr. at 5-47, 48). The research staff of Hibbard Brown talked to management at DreamCar, including Mr. Bianco, who previously had exclusive distribution rights for Lotus motor cars in the United States, and Gil Seasonwein, who had Big Three experience in Detroit in the area of product liability. (Tr. at 5-50, 51). Hibbard Brown staff also visited car dealerships selling DreamCar cars. Mr. Attalienti thought DreamCar had achieved "quite an accomplishment" by accumulating an inventory of 59 cars since these old cars were difficult to locate, necessitating a nationwide search. (Tr. at 5-56).

Reviewing the notice of allegations, Mr. Attalienti disputed the charge that Hibbard Brown had misrepresented or omitted any material facts in its communications with customers concerning the recommended securities. (Tr. at 5-57 to 5-132).

Mr. John B. Murphy, III, testified that he was employed by Hibbard Brown and had become familiar with when had called Murphy at his office. (Tr. at 5-203). asked Murphy to "[t]ell me about K.B. Communications," which made Murphy suspicious. (Tr. at 5-204, 210). Murphy did not recall having ever spoken to before called him. (Tr. at 5-205, 206). Murphy remembered call

because it had never before happened that someone not doing business with him would call and ask about a security. (Tr. at 5-210). He testified that called him at least twice, possibly three times. (Tr. at 5-211).

Murphy testified that he would never try to sell a security on an introductory call, and that even on a second call he would not try to sell a security because the purpose of a second call would be to determine customer suitability. (Tr. at 5-206, 5-207). If a potential customer had no interest in the stock market, Murphy would never call him again. (Tr. at 5-207). Murphy denied saying to that he did not have "the balls to make the decision to invest the $500 that was needed for this ground breaking opportunity of a lifetime." Murphy would never use that sort of language. (Tr. at 5-212).

During Mr. Murphy's direct examination, when asked at one point what was said during his telephone conversation with , Murphy responded with the question: "When he called me back?". On cross examination, when counsel for the State explored the possibility that Murphy had talked to before call, Murphy conceded, "I may have talked with him before." (Tr. at 216). He then stated that knew his name, had called him at work, and Murphy assumed that had Murphy's business card that Murphy had sent to him. (Tr. at 517).

Michael Martone testified that he is employed by Hibbard Brown, whose "speciality" is low-priced new issues and

over-the-counter stocks. (Tr. at 6-9, 15). On an introductory call to a prospective customer, he would hang up if the individual said he was uninterested in investing with Hibbard Brown. (Tr. at 6-9). If the individual were interested, Martone would ask a variety of questions for the purpose of determining customer suitability. (Tr. at 6-10, 13). The "philosophy" at Hibbard Brown is that "all stocks have risks." Every single common stock has risks. (Tr. at 6-14). Another part of the Hibbard Brown philosophy is to look for balanced portfolios "according to the client's needs." (Tr. at 6-15).

Martone testified that he attempted to sell "mutual funds and Nuveen tax-frees" but that wanted to invest in the stock market. (Tr. at 6-17). Martone told that low-priced new issues and over-the-counter stocks "were companies that had more inherent risks but through balanced portfolios there is potentially more reward in these areas as well." (Tr. at 6-17). was interested in these stocks, but showed no interest in receiving financial information about the companies Martone recommended. (Tr. at 6-17, 18).

When he visited , Martone brought along an issue of The Wall Street Journal to educate about the stock market and particularly the bid and asked pricing structure of securities. (Tr. at 6-21). described the $80,000 he had to invest as "play money," as opposed to his wife's IRA funds. (Tr. at 6-22). understood the difference between bid and asked prices. (Tr. at 6-32, 47). Martone specifically told him

the difference between the two prices is called the "spread," which will cause the investor to lose money if the bid and asked prices do not change. (Tr. at 6-33). Martone denied telling there were "no downside risks" when making recommendations. (Tr. at 6-34, 41, 51). He explained there are inherent risks in a "concept company." (Tr. at 6-34). He and discussed the "latest financials that would have been available at the time." (Tr. at 6-35). knew that Children's Creative was a "pink sheet" stock rather than a stock listed on an exchange. (Tr. at 6-39).

Martone and "talked about suitability every step of the way." (Tr. at 6-49). Martone said he does not make price predictions. (Tr. at 6-53). Hibbard Brown has a "fantastic research staff" and John Attalienti is "totally revered in our company." (Tr. at 6-57). Martone would not have told that Martone had information about a company that he could not divulge. (Tr. at 6-64). Martone would have told about any stock in which Hibbard Brown made a market, and such information would have been further disclosed on the confirmation slip. (Tr. at 6-66).

Brendan Hart testified that he is employed by Hibbard Brown in its Red Bank, New Jersey office, where his older brothers Michael Hart (also known as "Micky"), the national sales manager of Hibbard Brown, and Sean Francis Hart also work. (Tr. at 6-114, 188, 189). Brendan Hart testified that he had called and introduced himself, and was interested in

investing. (Tr. at 6-122). Hart and discussed investment objectives. said his short-term objective was speculating in individual stocks and he had a long-term growth objective. (Tr. at 6-123, 124). Hart testified that he met at his home and carefully reviewed the prospectus for Trans-Atlantic Video with . (Tr. at 6-127). told Hart that was a vice president of sales at the DuPont Company and that he did his banking at Wilmington Trust. Hart had known for two months. Hart recorded these items of information on the new account form. (Tr. at 6-129, 130). In reviewing the prospectus with Hart particularly pointed out the language stating that the investor should be able to afford the loss of his entire investment. was not deterred. (Tr. at 6-134). Hart also explained to the meaning of the term "warrant," which apparently understood. (6-135). Hart denied telling there were no downside risks to the Trans-Atlantic investment, but he may have told that could get his money out at any time and receive a check in a few days. That statement would have been true. (Tr. at 6-147).

Hart and discussed bid and asked prices many times, and understood the concept. (Tr. at 6-151). Hart thought he did a "very good job of due diligence" with respect to the Trans-Atlantic investment. (Tr. at 6-153). Hart never pressured to buy stock. (Tr. at 6-154). He did advise to diversify his investments. (Tr. at 6-156).

Hart gave a balanced view on every recommendation Hart made. (Tr. at 6-157). He told of the risks attendant to buying securities in a concept company, such as Children's Creative Workshop. (Tr. at 6-161). If Hibbard Brown had been a market maker in a security, Hart would have disclosed that fact, and the information would have appeared on the confirmation slip. (Tr. at 6-163). Hart discussed the "pros and cons" of each company he recommended, and he provided financial data and disclosed the associated risks. (Tr. at 6-172, 173). Hart does not use language such as "we are doing great" or "trust me." (Tr. at 6-183). testified falsely when he said that the actual value of his investments, as he learned on July 19, 1990, was far less than the value he was told by Hart on July 16, 1990. (Tr. at 6-187).

B. DeJuan Stroud testified that he is employed by Hibbard Brown as its director of compliance. (Tr. at 6-234). The compliance department at Hibbard Brown assists its officers, branch managers, and representatives to ensure there are no violations of the firm's supervisory procedures, NASD or SEC rules, or State rules and regulations. (Tr. at 6-236). The compliance department consists of a staff of nine, including seven professionals. (Tr. at 6-237). The staff reviews on a daily basis every new account report submitted to it from the branch offices. Each card must be complete, with no gaps. (Tr. at 6-240). Investment objectives must be substantiated for each customer. (Tr. at 6-242). All confirmation slips are similarly

reviewed on a daily basis. (Tr. at 6-243). All correspondence by customers and all customer complaints are also reviewed on a daily basis. (Tr. at 6-245).

The compliance department also undertakes a monthly review of customer account statements to make sure that the customer's account is diversified with growth stocks and conservative investments, or just with low-priced securities. (Tr. at 6-250). Additionally, the firm does an annual comprehensive review of each branch office during which Mr. Stroud will meet with every Hibbard Brown representative. (Tr. at 6-251).

II. SUMMARY OF THE SECURITIES AND DOCUMENTARY EXHIBITS

A. Children's Creative Workshop, Ltd.

This company was formerly Compass Resources, Inc., a basically inactive business that was intended to trade in Japanese artwork for its own account. (S-2 at 30). It liquidated its artwork at a loss of $124,500 and reorganized in July 1989, coming under the control of one Bernard Tessler. Mr. Tessler's earlier business effort called "The Enchanted Village" ended in bankruptcy and liquidation. Mr. Tessler's central concept for Children's Creative was to establish a store called "Our Childhood Dreams." This concept was "inspired" by his earlier effort, The Enchanted Village. (S-2 at 5).

The company had no operations or operating history in September and October 1989, and only one paid employee, Mr. Tessler. Mr. Tessler's salary during the year ended October 31, 1989 was $69,038, plus $10,758 received for expenses. He entered

into a five-year agreement with the company in July 1989 whereby he would be paid an annual salary of $150,000 with certain annual increases. Mr. Tessler was also entitled to an annual bonus of 10% of the company's pre-tax profits, plus an insurance policy valued at two million dollars to be paid by the company. (S-2 at 18, 33).

As of October 31, 1989, the number of shares of common stock outstanding was 20,393,300. The company issued 10,500,000 shares in connection with its July 1989 reorganization. As of February 14, 1990, Mr. Tessler owned 9,916,662 shares of common stock and owned the right with another shareholder to receive up to 7,500,00 additional shares if the company achieved certain minimum levels of net income. Mr. Tessler had acquired his shares in the July 1989 reorganization. (S-2 at 29).

In October 1989 the company issued 333,333 shares of common stock in lieu of paying $5000 on an outstanding loan. (S-2 at 29).

For the year ended October 31, 1989, the company incurred a net operating loss (on a consolidated basis) of $363,730. Its revenues for the year were $34,600 in consulting income. (S-2 at 26). Its total assets were $432,117, and it had an accumulated deficit of $371,419. (S-2 at 25).

On October 30, 1989, the company changed its independent certified public accountants from Mortenson and Associates, P.C. to Chesin & Company. The company then changed its accountants to Deloitte & Touche. The Form 10-K annual report for the year

ended October 31, 1989, stated that there had been no disagreement with the accountants. (S-2 at 16).

In September and October 1989 Mr. and Mr. each paid $1 3/8 per share for their shares of Children's Creative. At that price per share, the aggregate market value (number of shares outstanding times per share cost) of the company on October 31, 1989 would have been more than 28 million dollars. Investors paying that price per share would have been valuing the company at approximately 27.5 million dollars in excess of the company's total assets and at an infinite amount above the company's stream of net earnings, which were less than zero. Hibbard Brown acted in the capacity of a principal for each of these sales, selling the securities out of its own inventory. (S-67, S-68, S-70, S-81, S-82, R-38).

In its Form 10-Q financial report to the Securities and Exchange Commission ("SEC") for the quarter ended January 31, 1990, the company disclosed a net loss for the period of $78,999. Its revenues for the period were $2500 in consulting income. Its total assets had decreased to $338,694 and its accumulated deficit had increased to $450,418. The company disclosed that it had not yet opened the store based on its "Our Childhood Dreams" concept, and it did not have enough capital to open the store. It would not proceed with the project in the absence of additional financing. (S-3 at 9). The report stated that "the Company is not in a position to commence operating activities." (S-3 at 10). It further stated that it had no plans for any

additional financing arrangements and the "ongoing viability" of the company "will be threatened" in the absence of successful financing on favorable terms. (S-3 at 10).

All of the above-stated data on the company was public information by April 27, 1990, and was presumably in the hands of the Hibbard Brown research department, which regularly obtained and reviewed the Form 10-K and Form 10-Q financial reports of companies Hibbard Brown recommended. The Form 10-K financial report for the year ended October 31, 1989 was filed with the SEC on March 5, 1990. (S-2, R-25E). The Form 10-Q quarterly report for the quarter ended January 31, 1990 was filed with the SEC on April 27, 1990. (S-3).

In its May 14, 1990 Weekly Research Notes, Hibbard Brown stated the following in its comments on Children's Creative:

> The first prototype store is expected to be open by the end of summer for the back-to-school selling season. Although the store was originally due to be open this spring, management decided that due to the traditionally slow selling season during the summer it would postpone the opening to save the high fixed costs associated with carrying a new store during the summer months.

(S-33 at 4). At the top of the same page, the following statement appears in larger, bold-faced type: "We expect that CCW will open its first store in all three areas during the next 12 months." (S-33 at 4). Hibbard Brown was a market maker in this security at this time. That fact was not disclosed in its commentary on the company, however. Rather, it appeared inconspicuously in small italics on the back cover of the publication, which page otherwise contained no text other than a

branch office listing, research department personnel listing, and date of the price quotations. (S-33).

paid $10,318.50 for 7500 shares of Children's Creative. (S-67, S-68, S-70). They sold their shares on June 11, 1991 for a total of $373. (S-122). They lost $9,945.50, which was more than 96% of their investment.

paid $13,754 for their 10,000 shares of Children's Creative. (S-81, S-82). They still hold their shares, which are worthless. The company has changed its name to "Kent Holdings." (S-106).

B. Trans-Atlantic Video, Inc.

According to the prospectus for its initial public offering, which commenced on August 15, 1989, Trans-Atlantic Video was engaged in the marketing and sales of video cassettes to the budget home video market. (R-29C at 11). More than 70% of the titles in the program inventory were in the public domain. (R-29C at 13). The company had 14 full-time employees, four of whom were clericals. (R-29C at 14). The company's executive offices occupied 1200 square feet (the equivalent of one room 30 feet by 40 feet) on Route 33 in Freehold, New Jersey, costing $13,200 in annual rent. (R-29C at 14).

At the time of the initial public offering, the company was a defendant in litigation in Superior Court, Monmouth County, New Jersey, in which the plaintiff requested that a receiver be appointed for Trans-Atlantic because of its alleged inability to pay its debts on a timely basis. (R-29C at 14). According to an

independent auditor's report, the company had net income of $128,600 for the year ended December 31, 1988, and net income of $59,154 for the quarter ended March 31, 1989. (R-29C at F-4). As of March 31, 1989, its total stockholders' equity was $946,876, with a working capital (current assets minus current liabilities) surplus of $92,031. (R-29C at F-2, F-3).

The company's public offering was of 2,300,000 units, each unit priced at one dollar and consisting of four shares of common stock and two warrants. (R-29C at 1) Hibbard Brown was the underwriter, and it contracted to provide consulting services to the company over a two-year period. (R-29C at F-17). Prior to the offering, there were 5,350,000 shares of stock outstanding. (R-29C at 3).

bought 2000 units of Trans-Atlantic on August 15, 1989, paying $2000. On September 25, 1990, they sold the units at $1 1/4 per unit, for a total of $2498. They used the proceeds to purchase shares of Children's Creative Workshop. Hibbard Brown acted as a principal on the Trans-Atlantic sale, purchasing the units for its own inventory. (S-69, R-38).

In its Weekly Research Notes of February 19, 1990, Hibbard Brown recommended Trans-Atlantic as "an excellent way of playing the rapidly expanding market for the purchase of low price videos." (S-29 at 5). Hibbard noted that "[w]ith major contracts near completion the company appears poised for major expansion that would serve to increase shareholder value over the

long run." (S-29 at 5). On the back cover, in small italics, Hibbard mentioned that it made a market in the security. (S-29).

On March 5, 1990, bought 5000 shares of Trans-Atlantic common stock at two dollars per share, for a total cost of $10,002. On March 22, 1990, they bought an additional 5000 shares of Trans-Atlantic common stock at $2 1/8 per share, for a total cost of $10,627. Because of poor photocopying, the confirmation slips for these purchases put into evidence by the State do not reflect the capacity (whether principal or agent) in which Hibbard Brown acted. (S-75, S-76).

The Form 10-K annual financial report for the year ended December 31, 1989, which was filed with the SEC on April 16, 1990, shows that Trans-Atlantic's net sales had declined by $1,670,479 (18%) over those of the prior year. (R-29B at 13). The company suffered a net loss of $585,947. (R-29B at 12). Its full-time employees had declined to seven individuals, including three clericals. (R-29B at 8). Judgments had been rendered against the company in several lawsuits: $91,000 on November 13, 1989; $218,000 in April 1989; $174,000 in a case filed in December 1989, which judgment was vacated after a $20,000 payment by Trans-Atlantic and an agreement to take depositions to try to resolve the matter; and $103,000 in another action. (R-29B at 9-10). Trans-Atlantic did not bother to specify the lawsuits in which it was named as a defendant where the amount claimed did not exceed $50,000. Those lawsuits did not aggregate to more than $175,000, not counting interest. (R-29B at 10).

As of April 2, 1990, the company had 14,678,915 shares of common stock outstanding with an aggregate market value of $25,042,168. (R-29B at 1). As of December 31, 1989, its total stockholders' equity was $1,975,761. The initial public offering, completed in September 1989, had been successful: the company sold 2,300,000 units through Hibbard Brown and received $1,538,486 in net proceeds. (S-293 at 14).

In its Form 10-K annual financial report for the year ended December 31, 1990, filed with the SEC on April 29, 1991, Trans-Atlantic disclosed a share exchange and merger with Diamond Entertainment Corporation ("Diamond") whereby Diamond shareholders ended up owning 67% of the total shares of Trans-Atlantic common stock. (S-13 at F-18). The consolidated statement of operations for Trans-Atlantic and Diamond showed a net income of $110,319 for the nine-month period ended December 31, 1990. There were approximately 55 million shares of common stock outstanding, so that the net income per share was negligible. (S-13 at F-4). The company had a working capital deficit of $1,282,538 and owed $3,365,993 in notes to banks. (S-13 at F-2, F-3). The independent auditor's report stated that "the Company has suffered recurring losses from operations and has a net capital deficiency that raises substantial doubt about its ability to continue as a going concern." (S-13 at F-1). The Trans-Atlantic operation was down to five employees, one of whom was a clerical. (S-13 at 10).

sold their 10,000 shares of Trans-Atlantic on June 11, 1991, at one dollar per share, for a total of $9,998. (S-122). They had lost $10,631, which was approximately 52% of their investment.

C. Graystone Companies, Inc.

According to a Form 10-Q financial report for the quarter ended September 1989, Graystone was formed on January 4, 1989. It merged on June 16, 1989 with a company named "Easy Mergers, Inc." Graystone was in the business of providing pre-press publishing and marketing communications services. (R-33I at 8). According to an unaudited statement of operations, the company had a net loss of $270,859 for the nine-month period ended September 30, 1989. Its total assets were $603,470, and it had a working capital deficit of $168,583. (R-33I at 4-5). On December 31, 1989, the company had 2,005,899 shares of common stock outstanding. (S-20 at 17).

bought 1000 shares of Graystone on January 17, 1990, at nine dollars per share for a total cost of $9002. At that price per share, Graystone would have had an aggregate market value (number of shares outstanding times per share cost) of more than 18 million dollars. Investors paying that amount were putting a premium on the value of the company at least in excess of 17 million dollars over its total assets and an infinite amount over the company's stream of net earnings, which were less than zero. Because of poor photocopying, the State's exhibit of the confirmation slip does not show the

capacity in which Hibbard Brown acted when it made this sale. (S-74).

According to the company's Form 10-K for the year ended December 31, 1989, it suffered a net loss of $701,035. (S-20 at 16). Its total assets were $866,353, and it had a working capital deficit of $671,291. (S-20 at 15, 19). Four customers accounted for 70% of the company's revenues. (S-20 at 24). The independent auditor's report stated that the working capital deficit "raises substantial doubt about the Company's ability to continue as a going concern." (S-20 at 19). The company's "ability to continue its operations depends upon the realization of management's plans to generate significantly increased sales levels." (S-20 at 19). However, the report stated on a positive note, "Many of the resources needed to carry out such plans are already in place, including the hiring of additional sales representatives and the opening of additional facilities." (S-20 at 20). By the end of 1989, the company had 26 full-time and two part-time employees at its Waterbury, Connecticut facility. (S-20 at 5).

Hibbard Brown's Weekly Research Notes dated March 5, 1990, recommended Graystone as as an "attractive growth opportunity." (S-30 at 4). The Notes stated that Hibbard Brown believed that Graystone would be profitable in fiscal year 1990, even the first half of the year. The report stated that Hibbard Brown was "quite positive on the future for Graystone" and "we are optimistic about the future opportunities of Graystone." (S-20

at 4). On the back cover, in small italics, it was mentioned that Hibbard Brown was a market maker in Graystone stock. (S-20).

Hibbard Brown's April 23, 1990 Weekly Research Notes ("Notes") stated that Graystone had released its 1989 operating performance report the prior week, and that performance was "generally in line with anticipated results." (S-32 at 4). The Notes stated that Graystone reported "revenues of $1.55 million and net income of ($700,000)." (S-32 at 4). Hibbard Brown was again "quite positive" and "optimistic" about Graystone stock, in which Hibbard Brown made a market. (S-32 at 5).

Hibbard Brown again recommended Graystone stock in its May 28, 1990 Notes. It stated that the first quarter results ending March 31, 1990, were reported revenues of $627,914 and a net loss of $249,824. (S-35 at 2). The independent auditor's report dated March 23, 1990, for the year ended December 31, 1989, had stated that "[m]anagement estimates that sales levels of approximately four million must be attained in 1990 to cover anticipated operating expenses." (S-20 at 20). This report would have been available to Hibbard Brown at the time of its May 28, 1990 Notes. Graystone's first quarter 1990 revenues of $627,914 were substantially below its projected break-even level, which would have been one million dollars in sales per quarter. Hibbard Brown had the following comment:

> Importantly, although Graystone has yet to become profitable, the dramatic 140% increase in revenues were due to the continued focus on its marketing and sales efforts.

* * *

> We remain quite positive on the future for Graystone. We project revenues will more than double from the 1.55 million for fiscal 1989, and although the company was not profitable last year, we believe it can and will be profitable in fiscal 1990.

(S-35 at 2). If Graystone's 1.55 million dollar sales in fiscal 1989 doubled to 3.1 million dollar sales in fiscal 1990, the result would be a $900,00 loss according to Graystone's own projected break-even level in the independent auditor's report. (S-20 at 20). Hibbard Brown continued to make a market in the security. (S-35).

sold their shares of Graystone on March 5, 1990, at the urging of Brendan Hart. They sold their 1000 shares at $10 per share, for a net profit of $996. (S-74, S-80). Hibbard Brown did not send them a check, however. Instead, Hart directed to reinvest the money in Trans-Atlantic Video, which did. (S-75). About two weeks later, Hart told to buy 5000 more shares of Trans-Atlantic for $10,627, which did.

Graystone continued to lose money. Hibbard Brown's Weekly Research Notes dated September 24, 1990, reported that Graystone had lost its largest customer account and quarterly revenues had dropped to $413,301. (S-40 at 5). Hibbard Brown continued to make a market in Graystone, and it continued to recommend that its clients purchase Graystone: "[W]e consider the shares to be attractive at their current price." (S-40 at 6). At an asked price of $8 1/4 per share, an investor paying that price would

have valued the company at more than 18 million dollars since there were 2,267,491 shares outstanding. (S-40 at 5).

Hibbard Brown's explanation for its optimism was largely based on the fact that Graystone had reduced its work force by more than 65% to 13 employees. The Notes said, "This follows a consistent strategy of balancing both full-time and part-time personnel." (S-40 at 6). In fact, Graystone's new strategy of cutting its work force was entirely inconsistent with its strategy at the outset of the year. That strategy was to expand sales by hiring additional employees. (S-20 at 19-20, S-32 at 4).

Graystone suffered a net loss of $1,230,355 in fiscal 1990. Its total sales were $1,386,081--$166,875 below its fiscal 1989 sales. (S-21 at 16). Its total assets were $698,946 and it had a working capital deficit of $385,578. (S-21 at 15).

On September 9, 1990, Graystone borrowed $200,000 under a line-of-credit note from Hibbard Brown. (S-21 at 22). Substantially all of Graystone's assets were pledged to Hibbard Brown as collateral on the loan. Additionally, Hibbard Brown received 200,000 warrants as an inducement for the loan. (S-21 at 22).

In its December 17, 1990 Weekly Research Notes, Hibbard Brown continued to view Graystone's "shares to be attractive at their current price," which was an asked price of $8 per share. (S-45 at 5). Hibbard Brown no longer made a market in Graystone, however. (S-45).

D. DreamCar Holdings, Inc.

According to its Form 10-Q financial report for the quarter ended July 31, 1989, DreamCar Holdings was a development-stage company that changed its name from Access Capital, Inc., in July 1989 when it acquired American DreamCar, Inc. American DreamCar, the subsidiary, was formed in October 1988 for the principal purpose of "remanufacturing" and marketing "classic" American cars to the public. (R-26I). American DreamCar then had 60 cars in inventory, including six remanufactured cars. (R-26I). According to its unaudited statement of operations, the company had a net loss and accumulated deficit for the nine-month period ended July 31, 1989, of $214,053. On July 31, 1989, the company had 52,450,000 shares of common stock outstanding. As of July 31, 1989, the company had total assets of $2,108,829 and working capital of $1,670,562, primarily due to proceeds from an initial public offering. (R-26I).

On November 14, 1989, bought 5000 shares of DreamCar at $13/16 per share, for a total cost of $4,064.50. Hibbard Brown acted as a principal in the sale, selling the shares out of its own inventory. (S-83, R-38). With 52 million shares outstanding, a person paying $13/16 per share would value the company at $42,250,000, more than 40 million dollars in excess of its total assets and infinitely more than its stream of net earnings, which were less than zero.

DreamCar's Form 10-K annual financial report for the year ended October 31, 1989, showed that its net loss and accumulated

deficit had increased to $326,773. (R-26H at auditor's report 4). The company's total assets and working capital had declined to $2,008,456 and $1,437,702, respectively. (R-26H at auditor's report 2,3). Management stated its intention to sell its cars in the price range of $15,000 to $25,000 although one "investor/employee" had purchased a car for $3,426. (R-26H at 2, 11).

In its Weekly Research Notes dated February 12, April 2, May 21, and August 20, 1990, Hibbard Brown recommended that investors purchase DreamCar. (S-28, S-31, S-34, S-39). Its August 20, 1990 issue stated that "sales are moving at a moderate pace for a company of its size in what can be described as a poor year for the automobile industry." (S-39 at 3). Each of the Notes disclosed in small italics on the back cover that Hibbard Brown made a market in the stock.

In its Form 10-K report for the year ended October 31, 1990, the company disclosed that it had delivered its first car to a dealer in April 1990, but that it was unable to manufacture DreamCars on a profitable basis. (S-6 at 5). In October 1990 it had closed its paint and body shop and reduced its manufacturing work force from 21 employees to six. It reduced its headquarters staff to two employees, leaving a total of eight employees in the company. (S-6 at 5, 8). Due to financial constraints, it had defaulted on its rent payments for its headquarters offices, and the landlord had initiated eviction proceedings. (S-6 at 9).

During the year ended October 31, 1990, DreamCar had a net loss of $2,168,261. (S-6 at 13). Its total assets amounted to $907,246 and it had a working capital deficit of $421,827. (S-6 at 14). The company's independent auditor stated that there was "substantial doubt about its ability to continue as a going concern." (S-6 at F-1).

By March 31, 1991, the bid price for DreamCar had declined to $1/8 per share, making 5000 shares worth a total of $625. (S-90). By September 30, 1991, could not get a bid quotation for DreamCar, and his 5000 shares were apparently worthless. (S-106). lost their entire $4,064.50 investment in DreamCar.

E. Fireplace Manufacturers, Inc.

According to its Form 10-K annual financial report for the year ended March 31, 1989, filed with the SEC on July 5, 1989, Fireplace was in the business of manufacturing and selling metal fireplace systems. (S-14 at 2). In fiscal year 1989 it had net earnings of $524,645, up from $179,136 the prior year. In fiscal year 1989 it had sales of $20,146,510 and total assets of $7,840,450. (S-14 at 8). Although it was listed on NASDAQ, there was only a limited market for its stock and trading was sporadic. (S-14 at 6).

bought 2000 shares of Fireplace on August 24, 1989 at $1 1/4 per share, for a total cost of $2502. Hibbard Brown acted as a principal in the sale, selling the shares out of its own inventory. (S-66, R-38). On November 8,

1989, they sold their shares back to Hibbard Brown, which was again acting as a principal, for a total of $2623. (S-78). Rather than take their small profit in cash, however, they applied the proceeds of the Fireplace sale towards the purchase of shares in F. A. Computer Technologies, Inc. In doing so they followed the advice of their Hibbard Brown agent, Brendan Hart.

F. F. A. Computer Technologies, Inc.

According to its Form 10-K annual financial report for the year ended June 30, 1989, F. A. Computer Technologies, Inc. ("FACO"), was engaged in the distribution of microcomputers and computer peripheral equipment. (S-16 at 1). It purchased its products from manufacturers with which it had non-exclusive distribution agreements. (S-16 at 1). Despite a sales volume of 98 million dollars, in fiscal year 1989 it had a net income of only $1000. That was an improvement over its 1988 fiscal year net loss of $1,145,000. (S-16 at F-7).

FACO had raised its sales volume to 98 million in fiscal 1989 from 57 million the prior year mostly by acquiring Gates Distributing, Inc., on March 1, 1989. (S-16 at 14, 18). As a result of the acquisition, FACO's debt-to-equity ratio had risen from .77 in fiscal 1988 to 2.39 in fiscal 1989, and its working capital decreased from $4,614,000 to $2,085,000. (S-16 at 19).

In its Weekly Research Notes dated January 16, September 18, and October 9, 1989, and June 4, October 15, and December 10, 1990, Hibbard Brown recommended FACO to investors. It was

disclosed in small italics on the back cover of each issue that Hibbard Brown made a market in FACO securities.

On November 8, 1989, bought 10,000 warrants in FACO for $2,814.50. The warrants had an exercise price of one dollar per share of common stock and would expire on May 9, 1991. (S-71, S-17 at 1). Hibbard Brown acted as a market maker and a principal in the transaction. (S-71).

In its Form 10-K for the year ended June 30, 1990, filed with the SEC on September 28, 1990, FACO's statement of operations disclosed a net loss of $62,000 for fiscal year 1990. (S-17 at F-6).

The FACO price quotations in the Hibbard Brown Notes of December 10, 1990 are $1/4 per share bid and $3/8 per share asked. (S-44 at 3). 10,000 warrants, exercisable at one dollar per share, expired in May 1991. He and lost their entire investment of $2,814.50. (S-71, Tr. at 3-136).

G. Truvel Corporation

According to its prospectus dated January 29, 1988, Truvel developed and assembled computer peripheral equipment, primarily scanners, which it sold to original equipment manufacturers and system integrators rather than to end users. (R-27K at 3). The company had applied for patents on its scanners but had no assurance that its applications would result in the issuance of Letters Patent. (R-27K at 6). From its inception in June 1973 until late 1985, the company operated as an engineering consulting firm. (R-27K at 5). Although the company had net

income of $10,425 in 1984, it lost $48,018 in 1985, $479,598 in 1986, and for the nine-month period ended September 30, 1987, it lost $907,593. (R-27K at 12).

According to its Form 10-K annual financial report for the year ended December 31, 1988, filed with the SEC on April 3, 1989, Truvel's public offering in February 1988 was successful, resulting in $1,900,000 in net proceeds. (S-7 at 14). Nevertheless, the company suffered a net loss of $1,532,000 in fiscal 1988. (S-7 at 24).

According to its Form 10-Q financial report for the quarter ended July 1, 1989, filed with the SEC on August 15, 1989, Truvel suffered a net loss of $1,743,000 in the first six months of 1989. (R-27E at 2). For the same period, the company's cash flow was a negative $83,000, which would have been far greater had the company not issued $1,073,000 in common stock. (R-27E at 3).

At the recommendation of their Hibbard Brown agents, the and the invested in Truvel common stock in December 1989 within a day of each other.
bought 2500 shares of Truvel at $2 per share on December 19, 1989, for a total cost of $5002. (S-72).
bought 2500 shares of Truvel at $2 per share on December 18, 1989, for a total cost of $5002. (S-84). Hibbard Brown acted in the capacity of a principal in both transactions, selling the securities out of its inventory. (S-72, S-84, R-38).

Ten days later, on December 28, 1989, sold their Truvel shares at $2 1/4 per share, for a total of $5,623. (S-84). Ten days after their investment, on December 29, 1989, sold their Truvel shares at $2 1/4 per share, for a total of $5,623. (S-86). Hibbard Brown acted in the capacity of principal in both transactions, buying the securities back for its inventory. (S-84, S-86, R-38).

According to the Hibbard Brown agents, Martone and Hart, each of the purchases and sales by the and the were independent decisions by the investors. (Tr. at 6-58, 62, 88, 154, 155, 182, 212). The small profits on these transactions were not taken in cash by the and the , however. Rather, on December 28, 1989, used the proceeds of their Truvel sale to buy 3200 shares of Asset Growth Partners, Inc., at $ 1 3/4 per share, for a total cost of $5602. (S-85). On December 29, 1989, used the proceeds of their Truvel sale to buy 7500 shares of News Communications, Inc., at $3/4 per share, for a total cost of $5,627. (S-73). Hibbard Brown acted in the capacity of a principal in the purchase of Asset Growth Partners, selling the shares out of its inventory. (S-85, R-38). Hibbard Brown acted in the capacity of a market-maker and a principal for the purchase of News Communications, selling the shares out of its inventory. (S-73).

Truvel's Form 10-K annual report for the period of January 1, 1989 through September 30, 1989, filed with the SEC on April

17, 1990, showed a net loss of $4,987,000. (S-8 at F-5). The independent auditor's report stated that "the Company has suffered recurring losses from its operations...and continues to experience significant difficulty in paying creditors and has depleted its borrowing capacity and cash on hand as of April 6, 1990." (S-8 at F-2). The report expressed substantial doubt about Truvel's ability to continue as a going concern. (S-8 at F-3).

H. Asset Growth Partners, Inc.

In its prospectus dated November 9, 1989, Asset Growth stated that it was formed in 1983 under the name "USC, Inc.," and after going public in 1987 it came under the control of Steven Bingaman through a share exchange. (S-9 at 3). Asset Growth was a small merchant banking firm that owned and operated other companies, primarily its subsidiary Dynasound Organizer, Inc. (S-9 at 3). Asset Growth acquired Dynasound in April 1989 at a cost of approximately $3,833,000 which was financed primarily by debt. (S-9 at F-12). The consolidated financial statements showed a total debt of $3,573,026 for Asset Growth on June 30, 1989, and the auditor's notes stated that substantially all of Dynasound's assets were collateralized and the bank had imposed various restrictive covenants. (S-9 at F-16, F-17). On a consolidated basis, the statement of operations showed a net loss for Asset Growth of $490,729 in the year ended December 31, 1988. (S-9 at 12). The prospectus stated that "[t]he Company does not believe that there is a regular present [sic] established trading

market for its Common Stock and trading in the Common Stock of the Company has been sporadic and in small volumes." (S-9 at 14A).

On December 28, 1989, bought 3200 shares of Asset Growth at $1 3/4 per share, for a total cost of $5,602. (S-85). Hibbard Brown acted in the capacity of a principal in the sale, selling the securities out of its inventory. (S-85, R-38). During the next year, in its Weekly Research Notes of April 23, July 23, October 1, and December 3, 1990, Hibbard Brown recommended Asset Growth to its clients. In small italics on the back cover of each issue, Hibbard Brown disclosed that it made a market in Asset Growth securities. (S-32, S-38, S-41, S-43).

In its Form 10-K report for the year ended December 31, 1989, Asset Growth reported consolidated net income of $543,745. (R-28E at F-5). The company's total debt, long-term and current liabilities, had increased to $5,385,173. (R-28E at F-4). The report disclosed that Asset Growth and its president, Steven Bingaman, were defendants in a lawsuit where plaintiffs sought $3,000,000 and alleged that Bingaman had defrauded them by concealing the true value of another company and thereby fraudulently induced plaintiffs to enter into a stock purchase agreement. (R-28E at 15-16). Asset Growth continued to view trading in its stock as "sporadic and in small volumes," not a regular, established trading market. (R-28E at 21).

In October 1990, sold their 3200 shares of Asset Growth through Dean Witter. They sold at $3/8 per share, for a total of $1,077.65. (S-89). They had lost $4,524.35, which was approximately 81% of their investment.

In its Form 10-K annual report for the year ended December 31, 1990, Asset Growth reported a 56% drop in net income, to $234,463. (S-10 at F-4). Its total debt, long-term and current liabilities, had risen to $6,061,569. (S-10 at F-3). The report disclosed that Asset Growth's subsidiary, Dynasound, had been in violation of its restrictive covenants on December 31, 1990. (S-10 at F-15). The debt repayment schedule showed that in 1994 Asset Growth would face maturing debt obligations of $2,912,664. (S-10 at F-17). At the hearing the State's securities analyst, Mr. Minka, expressed doubt about the company's ability to meet its debt obligations. (Tr. at 1-107).

I. News Communications, Inc.

News Communications was formed in 1986 under the name "Applied Resources, Inc." for the purpose of offering a broad range of investment and financial services. It engaged in a "blank check" (no commitment as to the business or use of proceeds) offering in 1986, issuing nine million units of common stock and warrants. In 1987 News came under the control of Steven Bauman and Jerry Finkelstein through a share exchange with Access Network Corp., formerly Access Press, Inc., formerly G.D. Publishing, Inc. In 1988 and 1989 News acquired several

free-distribution weekly newspapers in New York, which formed the main activity of its business. (R-32J at 1-3).

News had never shown a profit, suffering net losses of $269,189 in 1985, $264,014 in 1986, $22,469 in 1987, and $174,390 in 1988. (R-32J at 11). According to its Form 10-K annual report for the year ended November 30, 1988, filed with the SEC on April 19, 1989, News had a working capital deficit of $246,599 at the end of fiscal 1988. Its independent auditor's report dated March 29, 1989, stated that "the Company has suffered recurring losses from operations and has a net working capital deficiency that raise substantial doubt about its ability to continue as a going concern." (R-32J at F-1). The company was involved in several lawsuits, and it reported that trading in its securities was "limited and sporadic." (R-32J at 7-9).

In its Weekly Research Notes dated July 31, 1989, Hibbard Brown recommended News to its clients as "an excellent opportunity for capital gains oriented investors." (S-24 at 3). The Notes stated that "the company's emerging profitability is very encouraging." (S-24 at 4). On the back cover of the Notes, Hibbard Brown disclosed in small italics that it made a market in the securities. (S-24).

In its Weekly Research Notes dated November 6, 1989, Hibbard Brown again recommended News. The Notes reported that "the growth forecast for this company is reaching fruition." (S-27 at 2). The Notes primarily focused on revenues and concluded with the following statement:

> Within the next 12-18 months we believe that News Communications can achieve annual revenues in the vicinity of $8 million, with increasing profitability, lending substantial attraction to the shares for long-term oriented investors.

(S-27 at 3). On the back cover of the Notes, Hibbard Brown disclosed that it made a market in News Communications securities. (S-27).

On December 29, 1989, bought 7500 shares of News common stock at $3/4 per share, for a total cost of $5627. Hibbard Brown acted in the capacity of a principal in the sale, selling the securities out of its own inventory. It disclosed this fact on the confirmation slip by the printed statement: "We make a mkt in this security." (S-73).

There were approximately 34,750,000 shares of common stock outstanding on November 30, 1989. (S-18 at F-8). Investors paying $3/4 per share would have valued the company at approximately 26 million dollars. At that value, investors were putting a premium on the company in excess of 25.5 million dollars over the company's net worth as stated in its Form 10-K filed with the SEC on April 19, 1989, and at an infinite amount in excess of the company's stream of net earnings, which were less than zero. (R-32J at F-2 to F-4).

In its Form 10-K report for the year ended November 30, 1989, filed with the SEC on March 15, 1990, News disclosed that in fiscal 1989 it suffered a net loss of $381,833 and its working capital deficit had grown to $928,339. (S-18 at 18). The independent auditor's report again expressed doubt about the

company's ability to continue as a going concern in view of its recurring losses and net working capital deficiency. (S-18 at F-1). The company disclosed that there had been only limited trading in its securities. (S-18 at 16).

In the Form 10-K report for the year ended November 30, 1990, filed with the SEC on March 15, 1991, News showed a net loss of $1,249,011. (S-19 at F-5).

On June 11, 1991, sold their shares (reduced to 2500 in a 3 to 1 reverse split) of News at $7/32 per share for a total of $544.88. (S-122). They had lost $5,082.12, which was 90% of their investment.

III. FINDINGS OF FACT

This section contains the primary findings of fact. However, all factual assertions in sections II, IV, and V are equally intended to be findings of the hearing officer. Section I, consisting of testimony, does not contain factual findings though it shows some of the evidence on which the findings are based.

A.

, a pipe fitter with a high school education, received an unsolicited telephone call from Michael Martone, an agent of Hibbard Brown, at place of work in Delaware. (Tr. 2-123, 126, 3-49). r said he was not interested in the stock market, but Martone continued to call him anyway. (Tr. at 2-126, 127). finally agreed to meet with Martone, who visited at his place of work. (Tr. at 3-57, 58).

had a lump sum of about $50,000 in proceeds from the sale of a personal residence. (Tr. at 3-63). He did not intend to risk the principal though he hoped to obtain a rate of return somewhat in excess of certificate of deposit interest rates. (Tr. at 2-143, 3-31, 55, 66). knew virtually nothing about the stock market, and he did not understand the term "market maker" or its significance. (Tr. at 2-125, 142). He did not understand at that time that low-priced, over-the-counter securities have a bid price and an asked price and that the spread between the two will cause an investor to lose a substantial amount of his principal if the bid price does not rise significantly.[4] (Tr. at 2-131, 132, 3-32, 72, 73). He did not understand that "pink sheet" (National Quotation Bureau listings) and low-end NASDAQ securities are thinly traded, so that it is possible for an investor in such securities to end up with worthless pieces of paper that no one wants to buy. (Tr. at 3-29; S-101 at 1410, 1422; S-105 at 243).

relied on Martone's advice as to appropriate investments and made that reliance clear to Martone. (Tr. at 3-28; S-103 at 5, 11). Mr. Martone dishonestly completed new account form, indicating that investment objective was speculation. (Tr. at 2-143; S-62). Martone then recommended that invest in Children's Creative Workshop.

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[4]This problem with the spread between bid and asked is far more important with thinly traded stocks (because the spread is much larger) than it is with New York Stock Exchange or NASDAQ National Market System (which is the "blue chip" echelon of NASDAQ) securities.

(Tr. at 2-130). (The details of all the investments are itemized in the foregoing section, which I adopt as my findings as to the particulars of the transactions).

Children's Creative was a highly risky security with little to recommend it, and Martone's recommendation was unreasonable and made in bad faith. (See section II. A., above). The security was unsuitable for in view of his intent not to lose principal and his lack of understanding of the investment. Martone did not disclose that, rather than being an objective adviser acting as a middleman, he and Hibbard Brown were acting in a principal capacity on the opposite side of the transaction with an undisclosed price mark-up. (My finding as to this nondisclosure by Martone is partially based on the cassette tapes, where Martone continues to pretend he is acting in best interests. See, e.g., S-103 at 11.) There was an inherent conflict of interest in Martone's advice, but he gave the impression he was acting in best interests. Martone even went so far as to assure that there was little or no downside risk. (Tr. at 2-131, 133). Martone falsely assured that Children's Creative would soon be listed on NASDAQ. (Tr. at 2-132). Martone downplayed the extraordinary risks inherent in this "pink sheet" stock by stating Hibbard Brown's "philosophy" that "all stocks have risks." (Tr. at 6-14). Martone failed to disclose the bid and asked pricing structure for the security, which he knew did not understand. (Tr. at 2-131, 132).

Throughout the pattern of trades that followed, did whatever he was told by Martone. (Tr. at 2-137 to 139; 3-28; S-103). Mr. Martone continued to recommend extremely speculative investments to , telling him on one occasion that he needed to make an additional purchase to obtain a "round lot." (Tr. at 2-133). Martone downplayed the risks and provided virtually no financial information other than promotional materials. (Tr. at 2-133, 135 to 137, 144; 3-32, 35; S-63). Martone himself knew little about the securities and was exclusively interested in selling them. (Tr. at 6-75 to 78, 81 to 87, 91, 93).

Mr. ended up with a portfolio of securities that were grossly overvalued at the prices paid and that traded only sporadically and in small volumes. The limited market for these "pink sheet" and low-end NASDAQ securities made them highly illiquid. (See section II, above; S-100; S-101; S-105). The profits made by r existed on paper, but Martone never suggested that pocket them. (Tr. at 2-138; S-103 at 8). Rather, the paper profits were highlighted by Martone to encourage to invest more. (S-103 at 6, 8, 12).

In December 1989 started to take a more active role, buying a book on the stock market, and in January 1990 he subscribed to an electronic bulletin board service on a computer. (Tr. at 2-140, 146, 3-34, 92). At that time became familiar for the first time with terms such as "bid," "asked,"

"spread," and "market maker." (Tr. at 3-32). As he grew suspicious of Martone, he started recording their telephone conversations. (Tr. at 3-23). In the taped conversations, showed his dependence on Martone and utter confusion about the nature of the investment world he had entered. (S-103 at 5, 12, 21, 41, 43, 47, 54, 62, 64). Martone, by his statements, demonstrated his awareness and encouragement of dependence and confusion. (S-103 at 10-11, 43). Having gotten to invest most of his money in extremely speculative stocks, Martone then encouraged to invest his wife's IRA money in a mutual fund through Hibbard Brown. (S-103 at 1-2).

Possibly because of complaint to the NASD or because disclosed to another Hibbard Brown agent that he was taping the calls, (S-103 at 61-62), some of Martone's conversations showed a belated attempt to create a record of full disclosure. (S-103 at 24, 26). (The chronology of the taped telephone conversations is unclear. See Tr. at 3-108, 109.). Habit taking over, however, Martone still did not get much beyond the disclosure that "all stocks have risks." (S-103 at 9). Only when he discussed the securities of potential competitors did Mr. Martone explain to some of the fundamental characteristics of the over-the-counter market. (S-103 at 39-40, 45, 52-53, 55). By that time had already committed his money, on Martone's advice, to a string of weak, overvalued

securities that resulted in the loss of most of his investment. (See section II).

On a cash-paid, cash-received basis (which has the effect of netting out the transactions where investments were liquidated and the proceeds were reinvested), lost $21,721.85 out of $22,820.50 invested, which was a 95% loss.

Subsequent to his investments with Hibbard Brown, as read about the stock market and exchanged information with other small investors on his computer, undertook to make several speculative investments on his own. (Tr. at 3-107, 108). These investments involved much smaller sums of money than the sums involved in his Hibbard Brown investments, and testimony was candid regarding these small speculations. (S-88 to S-90; Tr. at 3-107, 108). taped conversations with Martone help to show that the subsequent speculation was a departure from his earlier investment objective. (S-103 at 9, 16, 27, 46).

B.

is an individual with a high level of education in the science of chemistry, and he has been employed for most of his life in that area. (Tr. at 3-111, 112, 156 to 158). Like many individuals with a technical background, he knew nothing of the stock market or the financial world. (Tr. at 3-116). He did not even know the meaning of the terms "equity" and "warrant." (Tr. at 3-162, 165, 194).

received an unsolicited telephone call from Brendan Hart at home in Delaware. (Tr. at 3-114). Hart was an agent of Hibbard Brown who offered to sell securities to agreed to meet Hart, who visited at his home. (Tr. at 3-114).

was in danger of losing his job and he wanted to retire in about eight years, and he stated these facts to Hart. (Tr. at 3-120, 121, 6-198). Hart assured that Hart would provide him with good advice. (Tr. at 3-116). trusted Hart and was dependent on him, and Hart was aware of that dependence. (Tr. at 3-116, 192, 195). could tolerate a small gain or loss in the stock market, but he could not tolerate a substantial loss of principal. (Tr. at 3-121). He told Hart that fact and Hart understood it. (Tr. at 3-120 to 122). Hart dishonestly recorded investment objective on the new account form as "speculation" when it was not, (Tr. at 3-121, 187, 188; S-60), and Hart also falsified the statements of job title as "vp sale" and his bank as "Wilmington Trust." (Tr. at 3-177, 178; S-60).

Hart proceeded to recommend an investment in shares of Trans-Atlantic Video to (Tr. at 3-117). Trans-Atlantic was an extremely speculative investment. Like every other security that is part of this record, it had little or nothing to recommend it. (See section II. B., above). The investment was not suitable for in light of his investment objective (small growth or small loss), his personal

circumstances, and his lack of understanding of the nature of the investment and the risks he faced.

Although Hart gave a preliminary prospectus and a final prospectus for Trans-Atlantic at or around the time of investment, Hart did not encourage to read them. (Tr. at 3-181 to 185, 193). Nor did Hart orally discuss the salient points contained in the prospectuses. (Tr. at 3-189, 192). Rather, Hart repeated the Hibbard Brown "philosophy" to that all stocks have risks. (Tr. at 6-139). looked at one page of one of the prospectuses, did not understand the information, and did not bother to read any more. (Tr. at 3-134, 185, 190, 192, 195). His wife stored the prospectuses and subsequent issues of Weekly Research Notes from Hibbard Brown in folders, but the materials were never read. (Tr. at 3-208, 211, 214). relied upon the judgment and integrity of Brendan Hart. (Tr. at 3-116, 192, 195).

Hart's recommendation of Trans-Atlantic was unreasonable and made in bad faith, as were all of Hart's other recommendations to the (See section II. B., above). Hart himself knew little about the securities he sold, did not care about their characteristics, and was exclusively interested in selling them. (Tr. at 6-200, 203, 204, 208 to 211, 214, 215). He sold a portfolio of securities with similar characteristics of low net worth and virtually no net earnings, one by one, using the Hibbard Brown selling tactic of making the first sale and then urging investors to "diversify." (See section II, above; Tr. at

3-122, 6-156). (By this finding, I cast no aspersion on the investment theory of diversification that won Professor James Tobin a Nobel Prize in economics in the early 1980s). Hibbard Brown acted virtually every time as a principal or market maker, on the opposite side of the transaction, rather than as a neutral agent or middleman. (See section II, above). Hart never disclosed this fact, however. Rather, Hart made think that Hart was looking out for best interests. (Tr. at 3-116, 192). Hart called attention to paper profits to induce him to invest more money, which did. (Tr. at 3-132, 133, 140-141).

Other than the prospectuses for Trans-Atlantic, Hart provided with virtually no financial information other than promotional materials. (Tr. at 3-125, 127, 210, 211). (The Hibbard Brown Weekly Research Notes, which provide very limited and distorted financial information, are essentially promotional materials for those stocks in which Hibbard Brown makes a market. See section II, above.). Hart did not orally disclose even the most basic risks of any of the securities that he sold to . He did not disclose that the securities were extremely speculative and presented a substantial risk that would lose his entire investment. (Tr. at 3-118, 123, 126 to 133). He did not disclose the bid and asked pricing structure of the securities, or the fact that the substantial spread between the bid and asked meant that the investor would lose a substantial portion of his investment if the bid price did not rise

significantly. (Tr. at 3-118, 129, 131). He did not disclose the fact that the securities he sold to had a limited market and traded only sporadically and in small volumes. (See section II, above; Tr. at 3-122, 148 to 150, 154). Instead, when asked about liquidity, Hart falsely assured that it was not a concern. (Tr. at 3-122).

In his March 5, 1990 recommendation of Trans-Atlantic, Hart made the baseless forecast that the stock would become worth "a lot more than this $2," which was the price that paid per share. (Tr. at 3-132, 133). In his recommendation of Trans-Atlantic Video on March 22, 1990, Hart made the baseless forecast that the stock price "was really going to take off." (Tr. at 3-133, 134).

Hibbard Brown claimed at the hearing that its statement of its market maker and principal capacity on confirmation slips was adequate disclosure because the investors still had a right to rescind the transaction within two days. I find this disclosure on the confirmation slips to be insufficient because: (1) the investors were encouraged by their agents to view the agents as objective investment advisers looking out for their client's best interests, (2) the investors did not understand the meaning or significance of the terms "market maker" and "principal," (3) the term "market maker" on the slips was abbreviated to "mkt maker," and the principal capacity was conveyed by numeric code, making the message even more cryptic for an unsophisticated investor, and (4) the investors did not understand they had a right to

rescind within two days, and the confirmation slips did not explicitly state that. Rather, the confirmation slips stated: "This report of execution of your order shall be conclusive if not objected to in writing within two (2) days." (R-38 at back of sheet). Contrary to Hibbard Brown's argument about industry practice, I do not believe it is industry practice to mislead unsophisticated investors about the capacity in which a broker-dealer acts.

When told Hart that was losing his job and simply could not afford to invest any more, Hart did not give up. (Tr. at 3-139, 140). After hounding , Hart called wife to try to get her to change her husband's mind, but she would not. (Tr. at 3-6 to 9).

On July 16, 1991, telephoned Hart to learn the value of securities. Hart gave him figures for each, which calculated would cause a total loss of $5000. Three days later, on July 19, 1991, called Hart again and told him that wanted to sell all his securities. This time the figures provided by Hart caused to realize that his loss was in excess of $20,000. (Tr. at 3-141, 142). Hart had deceived as to the extent of his losses.

On a cash-paid, cash-received basis (which has the effect of netting out the transactions where investments were liquidated and the proceeds were reinvested), lost $26,237.12 out of $37,253 invested, which was a 70% loss.

C.

received an unsolicited telephone call from John B. Murphy, an unregistered agent of Hibbard Brown, on or

about March 19, 1991. (Tr. at 4-3, 4; S-49). Murphy called at his Delaware place of work and tried to sell him securities in a company named "K.B. Communications." (Tr. at 4-4). declined to do so, but he thought Murphy sounded like a "phony" and was concerned that investors might be defrauded by him. (Tr. at 4-7, 32). being a civic-minded citizen, called the Department of Justice and spoke to an investigator, Greg Gause. (Tr. at 4-6, 8).

Murphy subsequently called again, boasted that K.B. Communications had gone up to $7 3/8 per share, and berated Murphy for not buying the stock at $5 per share when he had the chance. (Tr. at 4-20, 21). Murphy hung up on , who called back just to inquire, ironically, whether they had been disconnected. (Tr. at 4-21, 22). Murphy then said he did not want to "mess with people that don't have the balls to put in the money that it takes to make a transaction like this go." (Tr. at 4-14, 21).

D. Hibbard Brown

The record in this proceeding reflects egregious misconduct by four different agents of Hibbard Brown: Michael Martone, Brendan Hart, John Murphy, and Sean Hart. At the time of his sales to , Martone had been employed by Hibbard Brown and its predecessor, Sherwood Capital, for at least one year. (Tr. at 6-5). Brendan Hart had been employed by First Jersey Securities, Inc., Sherwood Capital, and Hibbard Brown in the same office at Red Bank, New Jersey, since 1986. Moreover, Brendan

Hart held a Series 24 principal's license from the NASD, which is a prerequisite to supervisory responsibility. (Tr. at 6-112). Branch manager William Howard's testimony that there were six to eight Series 24-licensed assistant managers in the Red Bank office suggests that Brendan Hart might have been an assistant branch manager. (Tr. at 4-99). Although most of the violations occurred in the Red Bank office, near Hibbard Brown's New York headquarters, Murphy operated out of the West Palm Beach, Florida branch office.

My conclusion that there is a pattern of misconduct is supported by the role of Sean Hart in this case. Sean, an older brother of Brendan, had been previously employed by First Jersey Securities, Inc., and in connection with that employment he was named as a defendant in Delaware Court of Chancery Civil Action No. 8681, ultimately agreeing in 1989 not to apply for registration in Delaware for five years. (S-93; S-94 at 11). Sean Hart appears in this case as an employee of Hibbard Brown, assuring that he should not try to sell his securities because "fundamentally" the companies were "doing very, very good." (S-103 at 63-64). Hart made these statements on tapes in January or February 1990, when the companies were not doing well financially at all. The branch manager of Hibbard Brown's Red Bank office, William Howard, had been a fellow employee of Sean Hart at First Jersey and was aware of the consent agreement against Hart in Delaware. (Tr. at 4-117, 118, 120). Hart's conduct on the tapes shows that he was

unconcerned about being disciplined by Mr. Howard for engaging in further contacts with Delaware investors.

The discussion in section II above details the misleading recommendations and falsehoods contained in the Hibbard Brown Weekly Research Notes. Those falsehoods and misleading statements are consistent with the falsehoods and misleading statements provided to the Delaware residents and, indeed, to the hearing officer in this administrative proceeding. They form a pattern of dishonesty that I find is characteristic of this firm. I find as a fact that the conduct of Martone, Hart, and Murphy was encouraged, whether actively or tacitly, by the management of the firm.

IV. CONCLUSIONS OF LAW

A. Legal Standards

A *prima facie* case under section 7303(2) requires a showing that: (1) in connection with the offer, sale, or purchase of a security, (2) the respondent made an untrue statement of fact or failed to state a fact (3) that was material to the transaction. In the case of an omission, the necessity of stating the omitted fact is in part determined by the statements that were made by the respondent. If the statements that were made would convey a misleading impression of an important fact about the security in the absence of further disclosure, then the omission is material and there is a duty to disclose.

Generally, the test of materiality is whether a reasonable investor might have considered the information important when

making his investment decision. Affiliated Ute Citizens v. United States, 406 U.S. 128, 153-54 (1972). The Supreme Court has defined a material fact or omission as one that "would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available." TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976). This standard of materiality has been expressly adopted by the Third Circuit Court of Appeals as applicable to Rule 10b-5 cases. Sharp v. Coopers & Lybrand, 649 F.2d 175, 187 (3d Cir. 1981), cert. denied, 455 U.S. 938 (1982). The language and structure of Rule 10b-5 are nearly identical to section 7303, with the rule's subsections (a), (b), and (c) corresponding to section 7303's subsections (1), (2), and (3). See 17 C.F.R. section 240.10b-5 (1988).

Since the above-cited definitions of "materiality" are rather broad, there must be some limiting principle. I do not think that brokers are required to read orally a prospectus to an investor every time a sale is made. An important factor, though, is whether the broker acts as an order-taker or as an adviser recommending securities. The broker making a recommendation, especially of a low-priced, speculative security to an unsophisticated investor, must at a minimum provide a balanced perspective that includes the general contours of the downside risk. Where there is a substantial possibility that the investor may lose his entire investment, I cannot imagine a reasonable investor who would not consider that fact to be of critical importance. Of equal importance is whether there is a limited

trading market for the security, a fact that would present a substantial possibility that the owner may find no buyers for his security, making it worthless.

Additionally, the Delaware Court of Chancery has held that the meaning and potential effect of the spread between the bid and asked prices for a low-priced security and the fact of being a market maker for a recommended security are "plainly material considerations" that a broker is obligated to disclose. Flowers v. Hubbard, Del. Ch., Nos. 11915, 11916, slip op. at 7 (October 22, 1991).

Section 7303(2) requires that the misrepresentation or omission pertain to a "fact" rather than an "opinion," but in the securities context the term "fact" is often given the broadest interpretation reasonably possible. An excellent discussion of the modern rejection of the old doctrine of "puffing," as regards securities, may be found in Norville v. Alton Bigtop Restaurant, Inc., Ill. App., 317 N.E.2d 384, 389 (1974). The Illinois appellate court in that case noted that "recent authorities are unanimous in condemning the concept of 'puffing' in the context of securities regulation," and concluded that "[i]t is immaterial, then, whether the statements involved in this appeal are to be characterized as 'facts' or 'opinion.'" 317 N.E.2d at 389-90.

The Norville court's approach is supported by case law. In SEC v. Capital Gains Research Bureau, 375 U.S. 180, 194 (1963), the Supreme Court stated:

> There has also been a growing recognition by common-law courts that the doctrines of fraud and deceit which developed around transactions involving land and other tangible items of wealth are ill-suited to the sale of such intangibles as advice and securities and that, accordingly, the doctrines must be adapted to the merchandise in issue.

One court has stated that "where there is a question as to whether a given misleading statement is a statement of fact or merely an expression of opinion, it is likely that it will be found to be a statement of fact." First Mobile Home Corporation v. Little, Miss. Supr., 298 So.2d 676, 681 (1974), quoting 69 AM. JUR. 2d Securities Regulation section 102 at 1130 (1973).

Similarly, treatises and expert commentators have adopted this approach. 11C-Part 2 Business Organizations, SOWARDS & HIRSCH, BLUE SKY REGULATION section 6:04[1] at 6-80; L. LOSS, FUNDAMENTALS OF SECURITIES REGULATION at 717 (1988).

In particular, baseless recommendations and optimistic forecasts that have no grounds in historical fact are often treated as misrepresentations of material facts. Flowers v. Hubbard, Del. Ch., Nos. 11915, 11916, slip op. at 5 (October 22, 1991); Arrington v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 651 F.2d 615 (9th Cir. 1981); Mihara v. Dean Witter & Co., Inc., 619 F.2d 814 (9th Cir. 1980); Myzel v. Fields, 386 F.2d 718, 734 n.8 (8th Cir. 1967), cert. denied, 390 U.S. 951 (1968); Hiller v. SEC, 429 F.2d 856 (2d Cir. 1970); SEC v. North Am. Research & Dev. Corp., 424 F.2d 63 (2d Cir. 1970); Hanly v. SEC, 415 F.2d 589 (2d Cir. 1969); Fondren v. Schmidt, 626 F.Supp 892 (D.Nev. 1986); Norville v. Alton Bigtop Restaurant, Inc., Ill. App., 317

N.E.2d 384, 390 (1974); SEC v. Broadwill Securities, Inc., 240 F.Supp. 962 (S.D.N.Y. 1965). See also 11C-Part 2 Business Organizations, SOWARDS & HIRSCH, BLUE SKY REGULATION section 6:04[1] at 6-80.

The need for securities regulatory authorities to treat baseless recommendations and predictions as dishonest conduct is especially acute in the area of low-priced, highly speculative stocks that are sold over the counter ("OTC"). One expert has suggested that revocation of a broker-dealer's license on the basis of recommendations lacking a reasonable foundation may be one of the most effective weapons in combatting abuses in the OTC markets. Bloomenthal, Market-Makers, Manipulators and Shell Games, 45 ST. JOHN'S L. REV. 597, 626 (1971); Bloomenthal, The Case of the Subtle Motive and the Delicate Art--Control and Domination in the Over-the-Counter Securities Markets, 1960 DUKE L.J. 196, 220. Nowhere is the need for aggressive regulatory protection of investors greater than in the OTC markets. Rogoff, Legal Regulation of Over-the-Counter Market Manipulation: Critique and Proposal, 28 MAINE L. REV. 149, 159 (1976).

Subsection 7316(a)(7) provides a statutory basis for discipline where the applicant or registrant "has engaged in dishonest or unethical practices." Although this standard is written in general language, a general standard can be filled with content when the conduct at issue is judged in light of case law establishing prohibited conduct. See Selig v. Novak, Ark. Supr., 506 S.W.2d 825, 830 (1974) ("those charges which cannot be found in the statutes are covered by general language . . . and

reinforced by case law which has been developed over the years to protect the public from unethical conduct").

Generally, broker-dealers and their agents have the following duties with respect to nondiscretionary accounts: 1) the duty to recommend a stock only after studying it sufficiently to become informed as to its nature, price and financial prognosis, 2) the duty to carry out the customer's orders promptly in a manner best suited to serve the customer's interest, 3) the duty to inform the customer of the risks involved in purchasing or selling a particular security, 4) the duty to refrain from self-dealing or refusing to disclose any personal interest the broker may have in a particular recommended security, 5) the duty not to misrepresent any fact material to the transaction, 6) the duty to transact business only after receiving prior authorization from the customer, and 7) where the customer is unsophisticated about financial matters, the duty to define the potential risks of a particular transaction carefully and cautiously. Leib v. Merrill Lynch, Pierce, Fenner & Smith, 461 F.Supp. 951, 953 (E.D. Mich. 1978) (citations omitted).

The Delaware Court of Chancery has held that a broker may recommend a security only when he or she "(1) believe[s] in good faith that the investment is sound and appropriate for that customer and (2) has taken reasonable steps to inform himself or herself of the nature and prospects of the investment." Flowers, supra at 8.

Some federal courts have found that the securities industry's ethical standards as set forth in the NASD's Rules of Fair Practice ("NASD's Rules") constitute a sufficient basis for liability in a private tort action. SEC v. First Securities Co. of Chicago, 463 F.2d 981, 988 (7th Cir. 1972), cert. denied sub nom. McKy v. Hochfelder, 409 U.S. 880 (1972). Whether or not the NASD's Rules are a valid basis for a tort action, they certainly are valid evidence of ethical standards in the securities industry.

Probably the most pertinent of the NASD's Rules with respect to this case is section two, which states the following:

> Recommendations to Customers
>
> In recommending to a customer the purchase, sale or exchange of any security, a member shall have reasonable grounds for believing that the recommendation is suitable for such customer upon the basis of the facts, if any, disclosed by such customer as to his other security holdings and as to his financial situation and needs.

NASD MANUAL, Rules of Fair Practice para. 2152 (CCH).

Recommendations without reasonable historic justification are violations of section 7316(a)(7), in my opinion, rather than violations of section 7303(2). An unreasonable recommendation is an unethical practice rather than a misrepresentation of a material fact. (The statutory structure necessitates a distinction between the two). The legal proscriptions against (1) misrepresentations and omissions of material facts and (2) unreasonable or bad-faith recommendations constitute separate grounds for violations. The proscriptions have different goals. In the one case the recommendation of a completely inappropriate

investment vehicle is proscribed, whereas in the other the selling tactic of using falsehoods (regardless of the merits of the security) is proscribed. Thus, there is a legal distinction between a baseless forecast (e.g., "this stock is really going to take off"), which is fraud, and an unreasonable or bad-faith recommendation, which is unethical conduct.

Subsection 7316(a)(10), as amended by 68 Del. Laws, c. 181, effective August 16, 1991, states that a statutory basis for discipline exists where an applicant or registrant "has failed reasonably to supervise his agents if he is a broker-dealer or investment adviser, or an agent with supervisory responsibilities, and the Commissioner may infer such failure from an agent's violations." The responsibility to supervise must be interpreted broadly, for a broker-dealer's duty to supervise its employees is a "stringent" obligation. Rochez Brothers, Inc. v. Rhoades, 527 F.2d 880, 886 (3d Cir. 1975), cert. denied, 425 U.S. 993 (1976). The duty to supervise is an affirmative obligation on the part of a broker-dealer, which can be violated by negligent conduct, as opposed to violations of section 7303 and section 7316(a)(7), which require some form of intentional conduct by the management of a firm.

The existence of fraudulent intent and sham supervisory measures often can be deduced only from the "totality of events." Ruder, Multiple Defendants in Securities Law Fraud Cases: Aiding and Abetting, Conspiracy, In Pari Delicto, Indemnification, and Contribution, 120 U. PA. L. REV. 597, 635 (1972), quoting Trussel

v. United Underwriters, Ltd., 228 F.Supp. 757, 772 (D.Colo. 1964). See also Rolf v. Blyth, Eastman Dillion & Co., Inc., 570 F.2d 38, 47 (2d Cir. 1978), cert. denied, 439 U.S. 1039 (1978). A broker-dealer may not shield itself from the fraudulent acts of its employees by erecting a "Chinese wall" and relying upon sham supervisory procedures. See Sharp v. Coopers & Lybrand, 649 F.2d 175, 184 (3d Cir. 1981), cert. denied, 455 U.S. 938 (1982).

Finally, I note that some of my conclusions of law that follow do not precisely align themselves with the notice of allegations. In some instances the State charged Hibbard Brown and its agents with failure to disclose that the firm acted as a market maker in transactions with the Delaware investors. What was proven in most of those instances, however, was that Hibbard Brown acted as a principal in the transactions but not necessarily as a market maker. It is important to understand that the entire significance of a firm's acting as a market maker is that that status necessarily means that the firm acts as a principal selling out of its inventory. A principal (as opposed to an agent) is necessarily on the other side of the transaction from the customer, with an undisclosed price mark-up and directly adverse interests. The broker-dealer with an inventory of speculative securities that are thinly traded may have an incentive to "dump" the securities on unsuspecting customers, who subsequently find that they cannot sell the securities at a price anywhere near what they paid. (Such activity by an unscrupulous broker-dealer is commonly called a "hype and dump" scheme). On the other hand, one who acts in an agent capacity is relatively

neutral, acting only as a middleman and charging only a commission.

Thus, where the firm acts as a principal, its role as adviser to the investor is tainted. This fact is equally true regardless of whether or not the firm acts as a market maker. I believe that the respondents and their counsel were sufficiently sophisticated to understand this fact, and they understood that the gist of the allegation of being a market maker was that the firm acted as a principal with an undisclosed conflict of interest.

B. Violations Found

1. Michael Martone

Martone violated 6 Del. C. section 7316(a)(7) in each of his five securities sales to . He engaged in dishonest and unethical practices by willfully and in bad faith recommending four securities (two sales of Children's Creative, plus Truvel and Asset Growth Partners) to them that were unsuitable in light of their investment objectives. The DreamCar sale is not included as a suitability violation because conceded that he might have been speculating with his purchase of DreamCar stock. (Tr. at 3-38). Martone also engaged in dishonest and unethical conduct for each of the five sales by recommending securities without having done the due diligience research that was necessary to provide him with an adequate factual basis for an informed recommendation.

Martone also violated 6 Del. C. section 7303(2) and 7316(a)(2) in each of his five sales to . In connection with the two Children's Creative Workshop sales, he told there was little or no downside risk and the security would be listed on NASDAQ within several months. Both statements were misrepresentations of material facts. Martone also omitted to state material facts that were necessary to make his other statements not misleading. He failed to disclose the fact that Hibbard Brown was a principal in the transaction with an undisclosed price mark-up, and he failed to disclose the material fact of the bid and asked pricing structure which he knew did not understand.

In connection with the sale of DreamCar Holdings, Martone told that there was little or no downside risk to the investment. (Tr. at 3-32). This statement was a misrepresentation of a material fact. Also, Martone failed to disclose the material fact of the bid and asked pricing structure which he knew did not understand, failed to disclose the material fact that the security had a limited market and traded only sporadically and in small volumes, and failed to disclose the material fact that Hibbard Brown acted as a principal in the transaction with an undisclosed price mark-up.

In connection with the sale of Truvel, Martone told that there was little or no downside risk to the investment. (Tr. at 3-32). This statement was a misrepresentation of a material fact. Also, Martone failed to disclose the material

fact that the security was extremely risky and presented a substantial risk that would lose his entire investment.

In connection with the sale of Asset Growth Partners, Martone told that there was little or no downside risk to the investment. (Tr. at 3-32). This statement was a misrepresentation of a material fact. Also, Martone failed to disclose the material fact that the security had a limited market and traded only sporadically and in small volumes, and he failed to disclose the material fact that Hibbard Brown acted as a principal in the transaction with an undisclosed price mark-up.

In all, Martone committed 10 willful violations of the Delaware Securities Act. Although the plain language of 6 Del. C. section 7303(2) suggests that each misrepresentation or omission of a material fact is a separate violation, for purposes of convenience I will treat the numerous misrepresentations and omissions as one violation of section 7303(2) with respect to each sale. Similarly, I will treat the suitability and due diligence violations as one violation of section 7316(a)(7) with respect to each sale.

2. Brendan Hart

Hart violated 6 Del. C. section 7316(a)(7) in each of his 11 securities sales to . He engaged in dishonest and unethical practices by willfully and in bad faith recommending securities to them that were unsuitable in light of their investment objectives. He also engaged in dishonest and unethical conduct by recommending securities without having done

the due diligence research that was necessary to provide him with an adequate factual basis for an informed recommendation.

Hart also violated 6 Del. C. section 7303(2) and 7316(a)(2) in 10 of his 11 sales to . Ordinarily, a broker-dealer agent would be protected from claims of improper or inadequate disclosure by the giving of a current prospectus to an investor. Here, however, particular circumstances require a different result. knew nothing of the stock market and depended entirely on Hart, and Hart knew that. Misleading , Hart told that Trans-Atlantic was "a good buy." (Tr. at 3-116). Hart was aware that believed himself unable to understand the prospectus and that he was not likely to read it. Under these circumstances, Hart had the additional obligation of balancing his statement that Trans-Atlantic was a good buy with an oral statement of the degree of risk that faced. Hart omitted a material fact by not disclosing that the Trans-Atlantic securities were extremely risky and presented a substantial risk that would lose his entire investment. He also omitted a material fact by not disclosing the bid and asked pricing structure which he knew did not understand. Instead of providing a balanced perspective, Hart misled by telling him not to worry about liquidity, that when wanted to sell the security he would get a check in a few days. (Tr. at 3-122). Telling that there was no liquidity concern with Trans-Atlantic was a misrepresentation of a material fact. The lost 52% of their investment in Trans-Atlantic. They were

perhaps lucky that there were still market makers in the security. Otherwise, they would not have been able to sell it at all.

In connection with his March 5 and March 22, 1990 sales of Trans-Atlantic, Hart omitted to disclose to the material fact that the Trans-Atlantic securities were extremely risky and presented a substantial risk that would lose his entire investment.

In connection with the sale of Fireplace Manufacturers, Hart failed to disclose the material fact that Hibbard Brown acted as a principal with an undisclosed price mark-up, and he failed to disclose the material fact that there was a limited market for the security, which traded only sporadically and in small volumes.

In connection with the three sales of Children's Creative Workshop, Hart failed to disclose the material fact that Hibbard Brown acted as a principal in each transaction with an undisclosed price mark-up.

In connection with the sale of F. A. Computer Technologies, Hart failed to disclose the material fact of the bid and asked pricing structure which he knew did not understand, and he failed to disclose the material fact that Hibbard Brown was a market maker in the security, acting as a principal with an undisclosed price mark-up.

In connection with the sale of Truvel, Hart failed to disclose the material fact that the security was extremely risky

and presented a substantial risk that would lose his entire investment.

In connection with the sale of News Communications, Hart failed to disclose the material fact of the bid and asked pricing structure which he knew did not understand, failed to disclose the material fact that Hibbard Brown was a market maker in the security, acting as a principal in the transaction with an undisclosed price mark-up, and failed to disclose the material fact that there was a limited market for the security and that it traded only sporadically and in small volumes.

In connection with the sale of Graystone, Hart failed to disclose the material fact that the security was extremely risky and presented a substantial risk that would lose his entire investment. However, this omission was not charged in the Notice. Instead, the Notice alleged other omissions, such as the company's loss of $701,035 for fiscal year 1989. With each of the alleged omissions, however, there is a problem. It was not shown by the evidence that Hibbard Brown acted as a market maker or principal in this transaction. There was no testimony from concerning the bid and asked pricing structure. The fiscal 1989 loss, even if material, was not public information until after the sale was made. Therefore, I find no section 7303(2) violation in connection with this sale.

Brendan Hart committed a total of 21 violations of the Delaware Securities Act.

3. John B. Murphy

Murphy violated 6 Del. C. section 7313(a) and 7316(a)(2) by willfully offering to sell securities to a Delaware resident,

, on or about March 19, 1991, without being registered to sell securities in Delaware.

Although the State erroneously charged a violation of section 7314 in the Notice rather than a violation of section 7313, respondents and their counsel understood at all times that the gist of the alleged violation was that Murphy had offered to sell securities in Delaware when he was not registered to do so. For that reason I conclude respondents received adequate notice of the charge.

4. Hibbard Brown

Each of the above-stated violations by Hibbard Brown's agents, with the exception of the due diligence violations, also constituted a violation by the firm. Hibbard Brown thus committed 31 violations through the acts of its agents Martone, Hart, and Murphy. (Michael Martone's sale of DreamCar shares to does not constitute a violation of section 7316(a)(7) by Hibbard Brown because there was no suitability violation and the due diligence violation was by Martone only). As stated in section III above, I find that the pattern of dishonesty in the record of this case compels the conclusion that these agents acted with either the active or tacit encouragement of the managers and officials of the firm.

In addition to the 31 violations noted above, Hibbard Brown committed 17 violations of 6 Del. C. section 7316(a)(10) by failing to supervise reasonably its agents in connection with

their offers and sales of securities to Delaware residents. Each sale and Mr. Murphy's offer are counted as one violation each.

V. Remedies

The State has sought the revocation of the licenses of the respondents to sell securities in Delaware. Factors to consider in determining the appropriate remedies include the number of violations, the nature and circumstances of the violations, the number of investor victims, the amount of loss by the investors, the number of agents involved in the violations insofar as company liability is concerned, the history of the respondents, and whether the respondents have shown remorse or have attempted to correct the harm. Any sanction imposed for a violation must be proportionate to the underlying conduct. Blinder Robinson & Co., Inc. v. Bruton, Del. Supr., 552 A.2d 466, 475 (1989).

The number of violations is 10 by Michael Martone, 21 by Brendan Hart, one by John Murphy, and 48 by Hibbard Brown. With the exception of Murphy, each respondent committed a large number of violations. Although only two investors and a prospective investor were involved, Delaware is a small state and one would not necessarily expect to observe a large number of victims complaining about an unscrupulous firm. This is especially true when one considers that many victims of penny stock (and low-end NASDAQ stock) fraud never realize that they have been defrauded.

The nature and circumstances of the violations in this case were as egregious as securities violations can be without necessitating criminal charges. The investors were told numerous

falsehoods and given a false impression as to the nature of their investments. As a consequence, they suffered great financial injury. Looking at the investors' transactions on a cash-paid, cash-received basis (which has the effect of netting out the transactions where investments were rolled over),

lost $26,237.12 out of $37,253 invested, which was a 70% loss. On a cash basis, lost $21,721.85 out of $22,820.50 invested, which was a 95% loss.

The violations were by three different Hibbard Brown agents in two different branch offices. The worst violations were in the Red Bank, New Jersey office, which is near the firm's New York headquarters. The firm has been in operation and registered to sell securities in Delaware for approximately five years. On September 16, 1987, the firm and its president accepted findings by the NASD that Hibbard Brown had violated the NASD's Rules of Fair Practice and had violated a restriction agreement with the NASD. Under the agreement, Hibbard Brown was to limit its business activities to a general securities business consisting of retailing securities on an agency basis and an occasional transaction for its own account effected through another broker-dealer. Instead, Hibbard Brown listed itself as a market maker in five "pink sheet" securities and engaged in at-risk principal transactions. Hibbard Brown and its president consented to an NASD censure. (S-50 at Schedule D). Hibbard Brown has also been the subject of an administrative order in the State of Missouri that it cease and desist from effecting

transactions in over-the-counter, non-NMS (National Market System, the NASDAQ "blue chip" stocks) equity securities with a price of less than $5 except unsolicited orders to sell securities held long in customer accounts. (S-96). These violations outside Delaware are not very extensive, but the firm has not been in business for a long time.

The State has argued that this firm is in fact a transmutation of First Jersey Securities, Inc., a broker-dealer that was indicted by the New Castle County Grand Jury in 1986 for illegal sales to Delaware residents and agreed not to sell securities or apply for a license in Delaware until 1999. (S-92, S-94 at 7). The State pointed to the fact that Hibbard Brown's offices at Red Bank, New Jersey are physically the same as First Jersey's former offices, (Tr. at 3-119), that the telephone number is the same, (Tr. at 3-119), and that Sean Francis Hart, who appears on cassette tapes, was a First Jersey agent. (S-94; Tr. at 4-119). It also appears that B. DeJuan Stroud, the director of compliance at Hibbard Brown, was employed in the compliance department at First Jersey, (Tr. at 6-234), and that John Attalienti, director of research at Hibbard Brown, was director of research at First Jersey. (Tr. at 5-11). Michael Hart, the Hibbard Brown national sales manager at the Red Bank office, was a First Jersey employee, (S-47), and so was William Howard, the Hibbard Brown branch manager. (Tr. at 4-117, 118). It is possible that this firm is First Jersey in another form, but the State has not made any showing with respect to the

ownership code in Schedule A of the Form BD, and I decline to make that finding.

Finally, there is the question of whether the respondents have shown remorse or have attempted to cure the harm. Throughout this proceeding, I have observed not the slightest evidence that favors the respondents on this point. Rather than remorse, I have observed respondents' attempts to mislead the hearing officer in this proceeding. There is little doubt in my mind that John Murphy tried to convey a false impression in his testimony that had made first contact by calling him for the purpose of "setting him up." Murphy stated the following:

> Q. Now, why do you recall that conversation, that he called you?
>
> A. Because it's never happened before, someone that was not currently doing business with me.
>
> * * *
>
> A. Because he was quite suspicious. You know, I had never had anyone who was not currently doing business with me call up and ask about a security.

(Tr. at 5-210). After making a slip of the tongue during his direct examination, however, Murphy's testimony took a different direction on cross examination:

> Q. Is that what you meant when you stated earlier on your direct testimony, quotes when he called me back end quote? That you might have had a talk with him once before, before the time that he called you? Is that was you meant?
>
> A. He knew my name. He called me at work. I assumed he had my card that I had sent to him.

(Tr. at 5-217).

Similarly, Michael Martone's testimony was at times misleading if it was not outright perjury. Counsel for respondents argued that cassette tapes made a mockery of his testimony, but the mockery was of Martone's testimony. The falsehoods uttered by Michael Martone and Sean Hart on those tapes are too numerous to catalog here, but I will point to a few of them.

Martone testified at the hearing that he never made price predictions:

> Q. Did you predict that the price of its stock would go up quickly and reach $2 within a year as alleged in the middle of paragraph 27?
>
> A. No way. No, I would not make a price prediction like that. As a matter of fact, we don't make price predictions on these stocks. So there's no way I said that.
>
> Q. Have you ever made a price prediction?
>
> A. No. I don't make price predictions.

(Tr. at 6-53).

On the cassette tapes, however, Mr. Martone is heard to say the following:

> I saw DuPont hit 126 for the first time in a long time today.
>
> * * *
>
> It should hit 135 automatically.

(S-103 at 5).[5]

> I can have a nine to ten dollar stock in the next couple of weeks. Uh, I don't know when exactly it's going to make a move, but I've given you a nice early heads up.

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[5]Although I cite to the transcript, my quotations are taken directly from the tapes, S-102, as there were some errors in the transcription.

(S-103 at 6).

> Now we're talking about a company that has much stronger numbers and much stronger things happening but obviously now for me to double your money I got to have a stock making 10.2.

(S-103 at 9).

> Martone: [F]ind a couple of good guys who are looking for a winner. I'm have a nine, ten dollar stock that's going to be very very impressive.
>
> OK.
>
> Martone: Very very impressive.

(S-103 at 11).

> But I think if we do some positive things over the next couple of months and get the company listed, it should be able to jump right back to where we got it and it...as long as the company keeps doing the things they're doing business wise, it should be able to blow past it.

(S-103 at 22).

> Asset Growth Partners may not be, uh, a publicly held company for too long. There's...there's some rumors out there and we may by...we may be, uh, getting out of it, uh, because, uh, somebody's looking to engulf them. So, right now that's...that's on the rumor stage but there are talks going on that I know of. So, I'm...I'm sitting tight. I think something very very good can happen. Look, there's a couple of big players looking at the company.

(S-103 at 25).

> No, I don't see any more of a downside. Stock no...as far as I'm concerned this stock won't go down another penny, but I'll tell you one thing there's, uh, definitely got an upside.

(S-103 at 29).

> ...I expect DreamCar to make a charge up.

(S-103 at 37).

> These stocks are going to go back up. Well, Children's is definitely going to go back up....

(S-103 at 46).

The most obvious instance of Martone's mendacity was with respect to his explanation of his visit to the offices of Children's Creative Workshop. Apparently trying to impress with the quality of Hibbard Brown's research, Martone makes the following statements to on the tapes:

> Hey, let me let you know what's going on here. Friday and actually probably most of Thursday, we were up at Children's Creative Workshop.
>
> * * *
>
> So, we went up there. We sat down with the company. That's why I didn't get any of your messages on Friday. Actually I didn't get back into the office until this morning. So, uh, I would have given you a buzz on Friday only I...I hadn't seen your messages.
>
> * * *
>
> I think we're going to have to really push to get the company listed and that's what we were doing with the company. We were going all over their qualifications....

(S-103 at 20, 21). I find Martone's following testimony with respect to the tapes to be utterly dishonest:

> Q. And that goes on to say, "So we went up there. We sat down with the company." When did you sit down with the company?
>
> A. When I say "we," I'm not referring to me, I'm referring to Hibbard Brown.
>
> Q. Oh. And who from Hibbard, Brown had gone up there and sat down with the company?
>
> A. I really don't remember. That's what I wanted to clarify before, the "we" didn't necessarily mean me.
>
> Q. Well, it continues, Mr. Martone, the second line, "that's why I didn't get any of your messages on Friday."
>
> A. I see where you're saying. Is there a question?

(Tr. at 6-99).

Martone is also heard on the tapes giving the impression that Asset Growth Partners was listed on NASDAQ:

> : Because I've [inaudible] found that new one in the paper yet, the Asset Growth Partners.
>
> * * *
>
> How do they abbreviate it?
>
> Martone: Um, on the, on the quotron AGP, but in the, in the paper they may be, they might spell out the whole company or they may just abbreviate ASSP, GRWP, GWPH, PN partners, or PTN partners, or they may spell it out, but it'll be in alphabetic order. Look under NASDAQ and NASDAQ additional bid and ask.

(S-103 at 6-7). According to Mr. Attalienti, Hibbard Brown's director of research, Asset Growth Partners was never listed on NASDAQ. (Tr. at 5-182).

Other Hibbard Brown witnesses were evasive or misleading in their testimony. President Richard Brown emphasized that the brokerage is a "full service" firm, and he talked about municipal bonds and mutual funds, placing no particular importance on over-the-counter stocks. (Tr. at 4-84, 87). His agents, however, repeatedly stated that this firm "specializes" in low-priced stocks. (Tr. at 4-101, 6-15, 114, 118).

Mr. Attalienti, director of research, strained his credibility when he testified that political upheaval in eastern Europe formed an important basis for Hibbard Brown's recommendation of Trans-Atlantic Video (whose sales apparently never made it across the Atlantic). (Tr. at 5-86). Attalienti testified that the idea of Children's Creative competing with Toys-R-Us was "absolutely absurd," (Tr. at 5-46), but the company

itself disclosed Toys-R-Us as a competitor in its Form 10-K annual report to the SEC, (S-2 at 10), and Sean Hart is heard on Mr. tapes telling not to sell Children's Creative because he should remember the success of Toys-R-Us. (S-103 at 66).

Mr. William Howard, the branch manager, strained his credibility when he testified that he had learned of the existence of tapes only one week before the hearing. (Tr. at 4-120). Mr. Howard had earlier testified that he had six or eight assistant managers in the office who acted as his "eyes and ears." (Tr. at 4-93, 99). Sean Hart, a veteran Hibbard Brown employee, who happened to answer the telephone when called, knew about the tapes and knew enough about to tell him that he did not "have a case" in his complaint to the NASD. (S-103 at 61-62). Mr. Howard never knew about the tapes, however.

In sum, the testimony of the respondents in this proceeding has amplified my concerns about the dishonesty of the individuals at Hibbard Brown, and I see no evidence of remorse or any attempt to correct the harm that was done.

Intentional fraud by unscrupulous brokers selling extremely speculative, low-priced securities to unsophisticated investors has been a serious problem in the United States and in the State of Delaware in recent years. In the late 1980s the North American Securities Administrators Association estimated that penny stock fraud caused American investors to lose two billion

dollars each year. (S-100 at 1). The legislative history of The Penny Stock Reform Act of 1990 notes that this fraud constitutes a diversion of capital that would otherwise go to legitimate small businesses and, more importantly, it destroys investor confidence in the integrity of the marketplace. (S-101 at 1425). This type of fraud has been a major problem in the State of Delaware, as the Securities Division has previously revoked the licenses of Blinder, Robinson & Co., Inc.; Allied Capital Group, Inc.; Vanderbilt Securities, Inc.; F.D. Roberts Securities, Inc.; and Power Securities Corporation; in each case for defrauding Delaware investors of substantial sums of money. Although the respondents in this case argue that they no longer sell securities that come within the technical definition of a "penny stock," (See S-101 at 1428), the record in this case shows that they are equally adept at defrauding investors in low-end NASDAQ stocks, which they continue to sell.

For the above-stated reasons, the attached Order revokes the licenses of Hibbard Brown, Michael Martone, and Brendan Hart.

John B. Murphy has only one registration violation, and for that reason I will not impose a license revocation in his case. I note, however, that the circumstances of his violation are as egregious as they can be. Murphy berated for not buying securities, hung up abruptly, and insulted him by saying that he did not "have the balls" to make the transaction. Murphy's conduct was so extreme as to cause to worry about his fellow citizens being exposed to dealings with Hibbard Brown.

Moreover, Murphy gave deliberately misleading testimony under oath in the course of this proceeding.

Murphy's violation occurred in March 1991, which was after the statutory authority for administrative fines was raised from $1,000 to $10,000 per violation. 6 Del. C. section 7316(g), as amended by 67 Del. Laws, c. 274, effective July 2, 1990. The attached Order therefore imposes a fine of $5,000 and a 30-day license suspension on Mr. Murphy.

Because the violations (with one exception) by Hibbard Brown, Martone, and Hart were prior to the enactment of 67 Del. Laws, c. 274, effective July 2, 1990, the applicable maximum fine is $1,000 per violation for their violations. (The one exception is Hibbard Brown's violations of section 7313(b) and section 7316(a)(10) with respect to Murphy). Accordingly, the attached Order imposes fines of $10,000 on Michael Martone and $21,000 on Brendan Hart.

In the case of Hibbard Brown, I will not impose any fine for its supervisory violations. Although they are distinct from the fraud and suitability violations, an additional fine for the supervisory violations may seem excessive. Hibbard Brown shall pay a fine of $30,000 for 30 violations by its agents Michael Martone and Brendan Hart. (As noted above, one of Martone's violations of section 7316(a)(7) does not constitute a violation by the firm). Additionally, the firm shall pay a fine of $3,000 for its willful violation of section 7313(b) through its agent John Murphy. The attached Order imposes a total fine of $33,000 on Hibbard Brown.

The State has also requested the imposition of a restitution obligation on respondents Hibbard Brown, Martone, and Hart. The authority for such an order is unclear in that it would involve a retroactive application of the administrative restitution authority contained in section 7325(b), as amended by 67 Del. Laws, c. 274, effective July 2, 1990.

As a general principle, statutes in Delaware are not given retroactive application unless they clearly provide that they are to operate retrospectively. Chrysler Corp. v. State of Delaware, Del. Supr., 457 A.2d 345, 351 (1983). However, a distinction may be made between statutory provisions that alter substantive rights as opposed to procedural or remedial statutory provisions. Most Delaware cases refusing to give statutes retrospective application involve substantive rights. It is a common principle of statutory construction that remedial and procedural statutes may be applied retroactively:

> In many cases the idea is presented that statutes relating to procedure as distinguished from those relating to substantive rights are remedial. On this basis such statutes are given a liberal interpretation, since well-established personal or property rights are not affected. A common illustration of liberal construction of procedural statutes is found in cases giving them retrospective effect.

3A Sutherland Stat. Const. section 60.05 at 73-74 (4th Ed) (footnotes omitted).

There is some authority in Delaware in support of that principle. Monacelli v. Grimes, Del. Supr., 99 A.2d 255, 266 (1953) ("Statutory changes in practice and procedure are held to

be applicable to causes of action existing prior to the change."); Mergenthaler v. Asbestos Corp. of America, Del. Super., 534 A.2d 272, 277 (1987) ("Statutes which retrospectively make reasonable change in remedy are not impermissible.").

There is no question that securities laws are generally remedial and are to be liberally construed. Affiliated Ute Citizens v. United States, 406 U.S. 128, 151 (1972); Tcherepnin v. Knight, 389 U.S. 332, 336 (1967); SEC v. Capital Gains Research Bureau, 375 U.S. 180, 186 (1963); 3A Sutherland Stat. Const. section 60.02 at 61 (4th Ed) (legislation regulating business practices and requiring disclosure of information has been treated as remedial). However, it is probably inappropriate to generalize about the Delaware Securities Act as a whole. A number of cases have recognized that a statute may be both remedial and penal in nature, and its separate parts may require separate treatment. 3A Sutherland Stat. Const. section 60.04 at 68 (4th Ed). With respect to the Delaware securities amendments in 67 Del. Laws, c. 274, effective July 2, 1990, for example, the authorization for increased fines should not be applied retroactively.

The authorization for restitution is a different matter, however. The analysis of a prominent treatise on statutory construction suggests that a statute "is penal if it undertakes to redress a wrong to the public and remedial if it undertakes to remedy a wrong to the individual." 3A Sutherland Stat. Const. section 60.03 at 66 (4th Ed) (footnote omitted). Certainly,

restitution is in the nature of redressing a wrong to an individual. My analysis here is also influenced by the recent securities legislation in 68 Del. Laws, c. 181, effective August 16, 1991, which amended 6 Del. C. section 7301 to create a statement of purpose:

> (b) The purpose of the Delaware Securities Act is to prevent the public from being victimized by unscrupulous or overreaching broker-dealers, investment advisers or agents in the context of selling securities or giving investment advice, as well as to remedy any harm caused by securities law violations. This prophylactic and remedial purpose shall be deemed of paramount importance in the interpretation of the provisions of this chapter....

6 Del. C. section 7301(b).

For these reasons, I think the restitution remedy in section 7325(b) may be applied retrospectively, and the attached Order imposes an obligation upon Hibbard Brown to pay restitution to the investors. Additionally, Hibbard Brown shall pay the State for its costs of transcription of the hearing.

The above-stated remedies--license revocations for Hibbard Brown, Michael Martone, and Brendan Hart, and suspension for Murphy, the fines imposed on all respondents, and the obligation on Hibbard Brown to pay restitution and the State's costs of transcription--are all in the public interest and I so find. This firm and its employees present a clear threat to the financial well-being of the citizens of Delaware.

Richard W. Hubbard
Securities Commissioner

Date: February 13, 1992

BEFORE THE SECURITIES COMMISSIONER

OF THE STATE OF DELAWARE

IN THE MATTER OF:	)	
	)	
HIBBARD, BROWN & CO., INC.,	)	
MICHAEL MARTONE,	)	Case Nos. 90-01-02, 90-07-04,
BRENDAN D. HART, and	)	and 91-03-04
JOHN B. MURPHY,	)	
	)	
Respondents.	)	

ORDER

WHEREAS, a notice of allegations against the respondents was issued on June 19, 1991, by the staff of the Delaware Securities Division; and

WHEREAS, a hearing before the Securities Commissioner was held on the allegations during the period of October 28 through November 8, 1991, in the offices of the Delaware Department of Justice; and

WHEREAS, the respondents appeared at the hearing with counsel and contested the allegations; and

WHEREAS, it has been found that Michael Martone has willfully committed five acts of fraud, in violation of 6 Del. C. section 7303(2) and section 7316(a)(2), and has engaged in five acts of dishonest and unethical practices, in violation of 6 Del. C. section 7316(a)(7), in connection with his sales of securities to a Delaware investor; and

WHEREAS, it has been found that Brendan D. Hart has willfully committed 10 acts of fraud, in violation of 6 Del. C. section 7303(2) and section 7316(a)(2), and has engaged in 11 acts of dishonest and unethical practices, in violation of 6 Del.

C. section 7316(a)(7), in connection with his sales of securities to a Delaware investor; and

WHEREAS, it has been found that John B. Murphy has willfully committed one act of offering to sell securities in Delaware without being registered to do so, in violation of 6 Del. C. section 7313(a) and section 7316(a)(2); and

WHEREAS, it has been found that Hibbard Brown & Company, Inc., has willfully committed 15 acts of fraud, in violation of 6 Del. C. section 7303(2) and section 7316(a)(2), 15 acts of dishonest and unethical practices, in violation of 6 Del. C. section 7316(a)(7), one act of offering to sell securities in Delaware through an unregistered agent, in violation of 6 Del. C. section 7313(b) and section 7316(a)(2), and 17 acts of failing to supervise reasonably its agents in connection with their offers and sales of securities to Delaware residents, in violation of 6 Del. C. section 7316(a)(10);

IT IS HEREBY ORDERED that:

1. The broker-dealer registration of Hibbard Brown & Company, Inc., is permanently revoked.
2. The broker-dealer agent registration of Michael Martone is permanently revoked.
3. The broker-dealer agent registration of Brendan D. Hart is permanently revoked.
4. The broker-dealer agent registration of John B. Murphy is suspended for 30 days, commencing March 1, 1992 and ending March 31, 1992.

5. Hibbard Brown & Company, Inc., shall pay a fine of $33,000 on or before March 1, 1992.

6. Michael Martone shall pay a fine of $10,000 on or before March 1, 1992.

7. Brendan D. Hart shall pay a fine of $21,000 on or before March 1, 1992.

8. John B. Murphy shall pay a fine of $5,000 on or before March 1, 1992.

9. Hibbard Brown & Company, Inc., shall pay restitution in the amount of $21,721.85 to on or before March 1, 1992. This restitution payment obligation is conditioned upon the tender by to Hibbard Brown & Company, Inc., of any remaining legal or beneficial interest in any securities sold to them by Hibbard Brown & Company, Inc., or its agents.

10. Hibbard Brown & Company, Inc., shall pay restitution in the amount of $26,237.12 to on or before March 1, 1992. This restitution payment obligation is conditioned upon the tender by to Hibbard Brown & Company, Inc., of any remaining legal or beneficial interest in any securities sold to them by Hibbard Brown & Company, Inc., or its agents.

11. Hibbard Brown shall reimburse the State on or before March 1, 1992, or, in accordance with 6 Del. C. section

7324(a), as amended by 68 Del. Laws, c. 181, effective August 16, 1991, on or before the filing date of any appeal by Hibbard Brown of this Order to the Court of Chancery, whichever occurs first, for the State's costs of transcribing this proceeding.

12. The issuance of this Order is in the public interest.

Richard W. Hubbard
Securities Commissioner

Dated: February 13, 1992