

IN THE MATTERS OF  
MATES FINANCIAL SERVICES  
MATES MANAGEMENT COMPANY  
FREDERICK S. MATES

*File No. 3-2024. Promulgated March 9, 1970*

Securities Exchange Act of 1934—Section 15(b)  
Investment Advisers Act of 1940—Section 203(d)

**INVESTMENT ADVISERS ACT PROCEEDINGS**  
**BROKER-DEALER PROCEEDINGS**

**Grounds for Remedial Sanctions**

**Misrepresentations Concerning Investments in Restricted Securities and  
Performance of Fund**

**Misstatements to Clients and Prospective Clients Concerning Fees and  
Commissions of Registered Investment Adviser**

**Use of Inside Information in Purchase of Securities  
Manipulation**

Where officer and director of registered investment company, who was also officer and director of its investment adviser, caused company to acquire contrary to representation to shareholders, securities which could not be publicly offered for sale without first being registered under the Securities Act of 1933, to value such securities improperly under the Investment Company Act, and to redeem securities at prices based on such improper valuation; and held out performance of investment company to attract clients to registered investment adviser of which he was sole proprietor; and where such investment adviser received payments from brokers for directing brokerage business of managed accounts to them, effected purchases of stock prior to public release of material information relating to issuer, and engaged in manipulative activities with respect to such stock, *held*, in public interest to impose sanctions upon respondents pursuant to offer of settlement.

**APPEARANCES:**

*Allan S. Mostoff, David M. Butowsky and Herbert E. Milstein, and Michael S. Leo* of the New York Regional Office, for the Division of Corporate Regulation, and *Stanley Sporkin, Leonard H. Rossen and Stephen W. Arky*, for the Division of Trading and Markets, of the Commission.

*Milton V. Freeman and Werner J. Kronstein*, of Arnold and Porter, and *Harvey J. Klaris and Sheldon Curtis*, of Feiner, Klaris & Curtis, for respondents.

**FINDINGS AND OPINION OF THE COMMISSION**

We heretofore in these proceedings pursuant to Section 15(b) of the Securities Exchange Act of 1934 and Section 203(d) of the Investment Advisers Act of 1940 accepted an offer of settlement submitted by Mates Financial Services ("MFS"), a registered investment adviser; Mates Management Company ("MMC"), the investment adviser until August 5, 1968 to Mates Investment Fund, Inc. ("Fund"), a registered investment company;<sup>1</sup> and Frederick S. Mates, sole proprietor of MFS and president and a director of Fund and MMC. The order for proceedings alleged that in the period beginning in April 1968, among other things, Mates, contrary to representations to Fund shareholders, caused Fund to purchase substantial amounts of "restricted securities" which could not be offered for sale to the public without first being registered under the Securities Act of 1933, valued such securities improperly, and then held out to the public that the performance of the Fund was caused solely by the investment advice he furnished. The order further alleged that MFS and Mates allocated execution of securities transactions on behalf of MFS advisory clients to brokers who gave MFS and Mates substantial rebates, and that MMC and Mates purchased certain stock without disclosing material non-public information concerning the issuer and engaged in manipulative activities with respect to that stock.

Pursuant to the offer of settlement, an order was issued finding, for the sole purpose of these proceedings, that respondents willfully violated or willfully aided and abetted violations of various statutory provisions and rules as alleged in the order for proceedings. As provided in the offer of settlement, the order directed that Mates shall not become associated with a broker-dealer without our approval; suspended the registration of MFS as an investment adviser for a period of 100 days commencing at the opening of business on June 16, 1969, subject to the terms and conditions specified in the offer; prohibited MFS and Mates from issuing research reports and performing similar services for broker-dealers for

<sup>1</sup> Prior to August 5, 1968 Mates owned approximately 50 percent of the stock of MMC and on that date he acquired the balance. As a result, an assignment of the advisory contract between the Fund and MMC occurred and, as a consequence, the advisory contract terminated. Thereafter, Fund was managed by its officers and directors.

compensation without our prior approval; and prohibited the receipt by MMC of any fees from Fund for the first 60 days of any investment advisory contract which may be concluded between MMC and Fund.<sup>2</sup>

Respondents in their offer of settlement further consented to findings of violations as alleged in the order for proceedings, and we now issue our findings and opinion with respect to the issues in the case.<sup>3</sup>

#### INVESTMENT IN AND VALUATION OF RESTRICTED SECURITIES

Fund registered with us under the Investment Company Act on June 9, 1967 as a no-load diversified open-end management investment company. Since its inception Mates dominated the investment policies of the Fund. On February 7, 1968 Mates sent to Fund's shareholders along with the Fund's financial report dated January 31, 1968, a letter by him as president of Fund stating:

"In recent months, there has been a tendency among several mutual funds to take positions via 'investment letter' directly from the issuing companies or principal stockholders. This limits the liquidity of these positions since the shares so purchased must be registered with the Securities & Exchange Commission or held for a period of time before they can be resold to the public. Since 'investment letter' stock is generally available at a substantial discount from market, mutual funds which engage in this sort of activity can show quite remarkable results over the shorter term. Although we would not hesitate to step off the beaten path in search of unusual investment values, we believe that deliberately locking oneself into a position delegates too much of management's responsibilities to the vagaries of the market. Thus, you may be pleased to know that there is nothing in our portfolio that we could not sell immediately if we so choose."

Mates continued to mail the letter to new Fund shareholders through May 1968.

Despite the representations in the letter, between April 15 and July 23, 1968, Mates acquired for the Fund substantial amounts of various issues of restricted securities. Six of those

issues, which had an aggregate cost of \$3,610,000,<sup>4</sup> were assigned a value of \$7,161,250 when first placed in the pricing sheets for the purpose of determining the net asset value of the Fund. Four of the six securities were valued at the market price for unrestricted securities of the same issuer and class. Two, shares of stock of Omega Equities Corporation and of Giffen Industries, Inc., were valued pursuant to certain methods, which in effect resulted in a constant dollar discount from the fluctuating market price for the corresponding unrestricted shares.<sup>5</sup>

Because of bookkeeping and administrative difficulties, the Fund in June 1968 stopped issuing its own shares and undertook in the ensuing months to reconstruct its books and records. At about the same time the Fund borrowed more than \$7,000,000 from two banks and collateralized the loans with the Fund's entire portfolio. The borrowed money was used in part to purchase the restricted securities and in addition to satisfy Fund shareholders who presented their shares for redemption.

At no time during the period of April 18 through December 20, 1968, when as discussed below Fund applied to us for an order permitting it to suspend the right of redemption of its outstanding shares, was any disclosure made to the investing public of Fund's acquisition of restricted securities or its valuation procedures. Letters sent to the Fund shareholders in August and September 1968 made no mention of these facts, or of the Fund's borrowing of over \$7,000,000. During the April-December 1968 period, Mates gave at least three press interviews in which he referred to the market performance of Fund without adverting to the restricted securities. Thus, a story

<sup>4</sup> These six issues were:

Issuer	Securities	Cost
Bell Television, Inc. -----	15,000 shares \$60,000 bond convertible into 6,000 shares	\$ 90,000 60,000
Longchamps, Inc. -----	45,000 shares	405,000
Process Plants Corp. -----	\$25,000 bond convertible into 3,000 shares	125,000
Zimmer Homes, Inc. -----	50,000 shares	875,000
Omega Equities Corp. -----	300,000 shares	975,000
Giffen Industries, Inc. -----	36,000 shares	1,080,000
		3,610,000

Fund had in April 1968 also purchased 15,000 restricted shares of Oxford Financial Company for \$240,000, approximately 5.2 percent of Fund's assets at that time.

<sup>5</sup> During the period May 20 to November 28, 1968, the Omega stock was valued at a discount not exceeding \$2.75 per share from the market price of unrestricted Omega stock, and the Giffen stock was valued at a discount of \$6 per share. During this period brokers offered as much as \$34 and \$67 per share, respectively, for unrestricted shares of Omega and Giffen.

<sup>2</sup> Securities Exchange Act Release No. 8626; Investment Advisers Act Release No. 247 (June 12, 1969).

<sup>3</sup> Respondents have consented that in making our findings we may take notice of and use our public files and the testimony, exhibits and other materials obtained by our staff in its investigation of this matter.

carried in the New York Times on July 28, 1968, reported that Mates pointed out that Fund had appreciated more than 100 percent during the period of August 1967 through July 28, 1968.<sup>6</sup> During this same period Mates caused the Fund to publish its net asset value on a daily basis in various news publications throughout the country.

Mates continued through November 1968 to value the restricted securities as if they were unrestricted, except for the Omega and Giffen shares which, as noted, were valued at constant dollar amount discounts from the market price for unrestricted shares. As of November 26, 1968, the six issues of restricted securities were carried in Fund's portfolio at a value of \$13,459,000, more than \$10,000,000 in excess of their cost. As of that date, more than \$10,800,000 of the more than \$13,600,000 of indicated unrealized appreciation on all securities in Fund's portfolio represented indicated appreciation in restricted securities on the basis of the valuation procedures used by Mates.

On November 18, 1968 the accountants certified Fund's financial statements as of May 31, 1968.<sup>7</sup> On November 20, 1968 certain individuals brought suit against Mates and Fund alleging violations of the securities laws in connection with the Fund's acquisition of certain other securities. As a result of the ensuing publicity, the Fund's independent accountants, on about November 21, 1968, withdrew their certification of Fund's financial statement as of May 31, 1968. Thereafter Mates informed the accountants for the first time of the substantial acquisitions of restricted securities subsequent to May 31, 1968. Following this disclosure the accountants began a study of Fund's acquisition and valuation of restricted securities and at about this time the board of directors first gave special consideration to the valuation of Fund's restricted securities, and lowered the valuation of the six restricted securities on December 19, 1968 to \$11,576,085, or \$3,223,165 below the market price of the corresponding unrestricted shares.<sup>8</sup>

On December 20, 1968, we announced the issuance of an order temporarily suspending trading in the securities of Om-

ega pending clarification of information relating to Omega's financial condition, product lines and acquisition program and pending further inquiry with respect to whether that company's recent offers and issuances of its unregistered securities were in violation of the registration and antifraud provisions of the securities laws.<sup>9</sup> On the same day upon the application of Fund we issued an order permitting it to suspend the right of redemption of its outstanding redeemable securities.<sup>10</sup> In support of that application Fund referred to our suspension of trading in Omega securities and stated that such securities represented a substantial portion of Fund's portfolio and were held by Fund pursuant to investment letter,<sup>11</sup> and that such factors created a situation contemplated by Section 22(e) of the Investment Company Act of 1940.<sup>12</sup> Subsequently, we permitted resumption of trading in Omega securities, following the entry of a consent decree permanently enjoining Omega from violations of the Federal securities laws.<sup>13</sup> Thereafter, we rescinded the order permitting Fund to suspend the right of redemption of its shares, effective July 22, 1969,<sup>14</sup> and on the same date Fund resumed sales of its shares.

We have recently commented on the problems raised by the acquisition of restricted securities by investment companies.<sup>15</sup> Among other things, such acquisitions present problems of valuation, with the dangers that distortion in valuation will distort the prices at which the companies' shares are sold or redeemed and will indicate an investment performance that will mislead investors. In addition, since restricted securities may not be publicly sold unless they are first registered under the Securities Act, the acquisition of such securities reduces the flexibility and liquidity needed particularly by open end companies which are required to redeem shares within seven days on demand. These factors underscore the importance of full disclosure of an investment company's policy and practice

<sup>6</sup> Securities Exchange Act Release No. 8474 (December 20, 1968).

<sup>7</sup> *Mates Investment Fund, Inc.*, Investment Company Act Release No. 5571 (December 20, 1968).

<sup>8</sup> Restricted securities are sometimes referred to as "investment letter" securities because of the practice frequently followed by an issuer or a person in control of an issuer in selling such securities. —in order to substantiate the claim that the transaction does not involve a public offering and is within the so-called "private offering" exemption from registration under Section 4(2) of the Securities Act,—of requiring the buyer to furnish a so-called "investment letter" representing that the purchase is for investment and not for resale to the general public.

<sup>9</sup> Section 22(e) of the Investment Company Act provides, insofar as here relevant, that the right to redeem shares may be suspended for any period during which an emergency exists as a result of which disposal by an investment company of securities owned by it is not reasonably practicable or it is not reasonably practicable for such company fairly to determine the value of its net assets, or for such period as we may permit for the protection of securities holders of the company.

<sup>10</sup> Securities Exchange Act Release No. 8584 (April 24, 1969).

<sup>11</sup> Investment Company Act Release No. 5708 (June 12, 1969).

<sup>12</sup> Investment Company Act Release No. 5847 (October 21, 1969).

<sup>6</sup> During the entire year 1968 Fund was widely heralded as the country's leading performance Fund. Certain indices quoted Fund's appreciation during 1967 and 1968 as in excess of 170 percent.

<sup>7</sup> Pursuant to the request of the accountants, Mates and two other officers of the Fund provided the accounts on November 18 with a statement purporting to describe events subsequent to May 31, 1968 which would materially affect the Fund's financial position, but which did not mention the Fund's acquisitions of restricted securities after May 31, 1968.

<sup>8</sup> In the portfolio valuation as of November 26, 1968, the restricted securities had been valued at a discount of only \$882,000 from the market price of the corresponding unrestricted securities.

with respect to the acquisition and valuation of restricted securities.

Section 2(a)(39) of the Investment Company Act and Rule 2a-4 thereunder require that in determining net asset value, "securities for which market quotations are readily available" must be valued at current market value while other securities and assets must be valued at "fair value as determined in good faith by the board of directors." Readily available market quotations means reports of current public transactions or current public offers for securities similar in all respects to the securities in question. No current public transactions or current public offers can exist in the case of restricted securities. For valuation purposes, therefore, restricted securities constitute securities for which market quotations are not readily available. Accordingly, their fair values must be determined in good faith by the board of directors. Such a determination includes more than looking at the market values of the unrestricted securities of the same class. It requires an attempt to determine the inherent value of the securities, taking into consideration all relevant material and data, including current financial data of the issuer, and making adjustments for any diminution in value resulting from the restrictive feature.<sup>16</sup> The board of directors has a continuing obligation to make that determination at appropriate intervals throughout the period the restricted securities are retained in the investment company's portfolio.

In the instant case, during the period of April through August 1968 the Fund's board of directors did not even purport to value the Fund's holdings in restricted securities. In August 1968 the directors apparently were advised of Mates' valuation methods and made no objections. Mates continued through November 1968 to value those holdings at the market price for unrestricted securities of the same class or at a small discount from such prices, without regard for other factors which might have indicated lower valuations. Thus, it does not appear that Mates gave adequate consideration to the price paid by the Fund, the relationship between the amount of the restricted securities in Fund's portfolio and that of the freely traded securities, or the possible difficulties in reselling the restricted securities. Moreover, insofar as the Fund's Omega stock was concerned—which, as valued, comprised more than 20 percent

<sup>16</sup> The data and information considered and analysis thereof should be retained, so that they may be available for inspection by the company's independent auditors and our staff.

of the value of Fund's portfolio by late November 1968<sup>17</sup>—Mates knew that Omega was making other private placements of its restricted securities.<sup>18</sup> Prior to November 28, 1968 Mates valued Fund's holding in Omega at a discount of not more than \$2.75 per share, which at times during this period was less than 10 percent of the market price for unrestricted Omega stock.

In acquiring the securities described above, Mates followed a policy of orally committing Fund to purchase restricted securities, and then having the Fund value such securities in its portfolio at some subsequent date. During the period of April 15 through July 26 there were intervals of between 6 to 53 days between the time the Fund committed itself to purchase a restricted security and when it first included that security in its portfolio. In such intervals, the market prices of the unrestricted shares of several of the securities increased significantly, and such increases were reflected in the first valuations of the restricted securities in Fund's portfolio. Thus, Fund on July 8 agreed to purchase 300,000 restricted shares of Omega for \$3.25 a share, reflecting a discount of about 46 percent from the market price of approximately \$6 a share for the unrestricted stock of Omega.<sup>19</sup> However, Fund valued these securities in its portfolio for the first time on July 18, 1968, giving them a value of \$5.75 per share, the market price for the unrestricted securities having risen by that date to approximately \$8.125 a share. On May 31, 1968, Fund agreed to purchase 36,000 restricted shares of Giffen at \$30 a share, reflecting a premium over the then market price for the unrestricted stock of Giffen of approximately \$23.00 a share. However, Fund did not value these securities for portfolio purposes until July 23, 1968 when the market value for unrestricted stock had increased to \$58.00 a share, at which time the restricted stock was assigned a value of \$49.00 per share.<sup>20</sup>

The valuation of restricted securities at the market quotations for unrestricted securities of the same class, or at slight discounts from such quotations, is improper except in most

<sup>17</sup> As of November 26, 1968, Fund reported net assets of \$25,378,798.

<sup>18</sup> See Securities Exchange Act Release No. 8584 (April 24, 1969). The private placements were generally at discounts of 50 percent from the market price for unrestricted securities. Because of increases in market prices in the intervals between the times agreements to purchase Omega shares were signed and the dates sales were actually consummated, the prices actually paid were approximately 25 percent of market prices on the dates the stock was acquired.

<sup>19</sup> The market price for unrestricted Omega stock increased from approximately 60¢—70¢ a share on April 30, 1968 to about \$33—\$35 per share on December 9, 1968. In February 1970 such stock was at about \$.75—\$1.00 per share.

<sup>20</sup> Portfolio valuations of the Giffen stock on all other dates through November 26, 1968 were at a discount of only \$6 per share from the market price, in accordance with the method used by Mates.

unusual circumstances not present here. The valuation procedures followed by Mates not only gave the Fund, whose investment policy and attendant publicity stressed performance, the appearance of a greater appreciation in value than was justified had proper valuation procedures been followed, but the delay in valuing the restricted securities in the Fund's portfolio showed such appreciation to have been achieved over shorter periods of time than was actually the case. There was thus created a distorted picture of the Fund's performance which affected investors' decisions to redeem or to continue to hold their shares. The Fund's reported net asset value rose from approximately \$9 a share in early June 1968, when the Fund stopped sales of its shares because of the back office problems, to \$16.88 a share in early December of that year. To the extent that such asset values were inflated by the Fund's improper valuation procedures, holders who did not redeem their shares were also adversely affected as a result of redemptions that were made by some 300 shareholders during this period at redemption prices based on those asset values.<sup>21</sup>

The importance of a full disclosure with respect to the acquisition of restricted securities and the possible consequences thereof is further underlined by the other serious problems which confronted the Fund in this case. By November 1968, more than 20 percent of the Fund portfolio assets as valued by Mates were in Omega stock and an additional 22 percent were in other restricted securities. The Fund thereby became dependent upon developments in the affairs of several of its portfolio companies and at the same time lost much of its flexibility with respect to choosing securities which could best be sold where necessary to meet redemptions. Moreover, on December 20, 1968, when we suspended trading in Omega stock, the Fund was unable to value its portfolio. As we already noted, it therefore had to suspend redemptions of its outstanding shares.

Thereafter, in order to put itself in a more liquid position and also to obtain cash to pay off the bank loans of approximately \$7 million, the Fund was forced to sell a number of restricted securities at prices substantially less favorable than the portfolio values previously assigned to them.<sup>22</sup> For example, Fund sold its Giffen holdings at \$41 per share on December 31, 1968, only a little over a month before a registration statement

which included those holdings became effective under which Giffen shares were offered at \$55 per share. The \$41 price obtained by Fund on December 31 was approximately \$11 per share less than the portfolio figure as of December 19 (the day before the suspension of redemption rights) and only about two-thirds of the market price of unrestricted Giffen shares as of December 31. Also on December 30, 1968, the Fund sold its holdings in Longchamps, Inc. at \$25 per share, being almost \$12 less than their portfolio valuation as of December 19 and reflecting a substantial discount from the market value of the unrestricted stock as of December 30.

In July 1968, after the Fund ceased selling its shares, MFS, a sole proprietorship wholly owned by Mates, registered as an investment adviser. Wide publicity accompanied the opening of this business. In addition, Mates provided prospective clients of MFS with material emphasizing the performance of the Fund. Mates and MFS continually brought to the attention of prospective clients of MFS that Fund had the highest reported performance of any registered investment company in the United States. During the period of July through December 1968, MFS and Mates told investors who inquired about investing in the Fund that the Fund was not then selling its shares but that MFS would provide the investor with management similar to that provided to the Fund. The Fund's apparent performance was thus used to lead investors to believe that with MFS's advisory management their own investments would also produce spectacular results. In the period of July through December 20, 1968, a total of 717 individuals became clients of MFS, entrusting to MFS and Mates more than \$17,000,000.

In summary, contrary to his representation to Fund shareholders that the Fund would not acquire securities which could not be sold without registration under the Securities Act, Mates caused the Fund to acquire substantial amounts of such securities. In so doing, he created a situation which could adversely affect the ability of the Fund to comply with the requirements of the Investment Company Act relating to the Fund's shareholders' rights of redemption, contrary to the representations with respect thereto. Thereupon Mates improperly valued such restricted securities in the Fund's portfolio in violation of the valuation provisions of Sections 2(a)(39)(B) and 22(e) of the Investment Company Act and Rule 2a-4 thereunder, and thereby misrepresented to Fund shareholders and to clients and prospective clients of MFS the extent and the cause of the reported increase in the Fund's net

<sup>21</sup> In this period approximately 160,000 shares were redeemed for about \$2,100,000.

<sup>22</sup> We have recently pointed out some of the dangers of acquiring restricted securities. See Investment Company Act Release No. 5846, *supra*, p.6.

assets and net asset value per share. We conclude that in these respects, Mates and MFS willfully violated or willfully aided and abetted violations of the antifraud provisions of Sections 206(1) and 206(2) of the Investment Advisers Act and of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

#### REBATE PRACTICES

During the period July-October 1968, MFS and Mates also willfully violated Sections 206(1) and (2) of the Investment Advisers Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, in that they allocated the execution of securities transactions on behalf of MFS advisory clients to brokerage firms which gave MFS and Mates rebates. These rebates took the form of payments purportedly for an investment advisory publication of MFS and were made contrary to representations to the clients with respect to fees and commissions.

By October 1968 MFS was the investment adviser to over 700 clients for whom Mates made investment decisions on a discretionary basis. A brochure distributed to clients and prospective clients of MFS stated that MFS was not a broker and collected no commissions on clients' accounts; that MFS's fee was based on the net value of a client's portfolio; and that such fee was paid out of the client's account every quarter at rates of  $\frac{1}{4}$  of 1 percent to  $\frac{1}{2}$  of 1 percent of the client's equity depending on the amount of such equity.

MFS also published an advisory service for brokers for a monthly fee of \$5,000 (subsequently reduced to \$3,000) which offered subscribers five or six research reports per month, individual reports on specific securities on request, and seminars to be conducted by Mates. However, very few brokers requested special reports and no seminars were held. The advisory reports that were furnished were merely rather brief market letters, each of which covered one recommended security and presented a very general description of the issuer and its assets with a minimum of financial information. The principal aspect of the arrangement with brokers subscribing to the service was that they were given to understand that if they subscribed to the Mates advisory service, they would be allocated brokerage business arising from the accounts managed by MFS from which they could realize substantial commissions. During the relevant period, MFS allocated a substantial number of brokerage transactions in the accounts of its clients to seven broker-dealer firms and two registered representa-

tives who subscribed to the Mates advisory service. During that period the subscription payments received from such firms and representatives exceeded \$90,000, which was more than twice as much as MFS received during the same period from the fees charged clients for managing their investment accounts.

It is evident that the subscriptions offered to brokers were a subterfuge for obtaining rebates from such subscribers in connection with commissions generated by transactions in the portfolios of clients whose accounts were managed by MFS, and the omission to disclose such commission rebates made misleading the representations to clients that no commissions would be collected on their accounts and that MFS annual investment advisory fees would not exceed 2 percent of the equity in their accounts. Moreover, MFS and Mates were fiduciaries in their relationship to their clients in that they acted as investment adviser and directed the execution of securities transactions for them. The arrangement with subscribers to the broker advisory service that they would receive orders for transactions in the accounts of MFS clients enabled MFS and Mates to derive undisclosed personal benefits from the clients. It gave MFS and Mates a personal interest in the volume of the transactions and the selection of executing broker which conflicted with the duty of serving only the clients' best investment interests. The abuse of position and conflict of interests inherent in the making of such arrangements were inimical to the MFS clients.<sup>23</sup>

#### USE OF INSIDE INFORMATION

During April 1968, MMC and Mates willfully violated Section 17(a) of the Securities Act and Sections 9(a)(2) and 10(b) of the Exchange Act and Rule 10b-5 thereunder, in the purchase of shares of common stock of Ramer Industries, Inc., which were listed on the American Stock Exchange. MMC and Mates obtained through a Ramer director certain non-public material information concerning a rise in the sales, earnings and earnings projections of Ramer. They thereupon purchased Ramer stock without disclosing the information, then disclosed the information to certain registered representatives and others who also purchased Ramer stock without disclosure, and engaged in manipulative activities with respect to Ramer stock.

During the first quarter of 1968, Ramer's financial position and prospects improved significantly, Ramer's sales for that

<sup>23</sup> Cf. *Consumer-Investor Planning Corporation*, 43 S.E.C. 1096 (1969).

quarter being its highest on record. Whereas Ramer had shown a \$.03 per share loss for the first quarter of 1967, a press release issued April 16, 1968 estimated first quarter 1968 earnings for Ramer at \$.15 per share, and on April 17, 1968 actual first quarter earnings of \$.16 per share were announced.

The minutes of the April 3, 1968 meeting of the Board of Directors of Ramer recited that the treasurer of the company reported on the first quarter's earnings and that the Board expressed pleasure with the results. A director of Ramer, who had attended the meeting, began purchasing Ramer stock for his own account the following day. On April 9, 1968, Mates met with that director, who was a registered representative with a broker-dealer firm and with whom Mates had a close relationship, and in the three following business days, Mates placed orders with the director for the purchase of a total of 27,000 shares of Ramer stock on behalf of the Fund and two other mutual funds. Prior to this time none of the three funds had ever transacted any business with the Ramer director.

Mates also spoke to certain registered representatives who generally followed his recommendations, and told them that he was buying Ramer stock, that Ramer's earnings would be up and that Ramer was a turn-around situation. As a result of this recommendation and the purchase activity that had already taken place, Mates was able, directly or indirectly, to induce the purchase by these representatives for their clients of approximately 65,000 shares of Ramer prior to the public announcement of the 1968 first-quarter earnings. Thereafter Mates continued to recommend Ramer stock and induced purchases of the stock.

Ramer had approximately 750,000 shares of stock outstanding as of April 1, 1968. During March 1968 and the first few days of April, trading in Ramer stock on the American Stock Exchange amounted to about 1,000 shares or less per day. In the three week period ending May 3, 1968, the total volume of trading in Ramer stock on the exchange was 1,169,000 shares, and during this period the price of the stock rose from about \$5<sup>3</sup>/<sub>8</sub> to \$14 per share. Mates through his own transactions and his recommendations to others was responsible directly and indirectly for the purchase of at least 151,000 shares of Ramer stock during the last three weeks of April 1968 and was thereby able to affect appreciably the market value of the Fund's portfolio holdings of Ramer stock.

It is clear that through his relationship with a director of Ramer, Mates had access to non-public material information

which he used for his own advantage and that of his clients.<sup>24</sup> This information was of such importance that it could reasonably be expected to affect the judgment of investors whether to buy, sell, or hold the stock. If generally known, such information could reasonably be expected to affect materially the market price of the stock.<sup>25</sup> We concluded that Mates' and MMC's advance use in market purchases of the favorable information concerning Ramer for their own or their customers' benefit and to the detriment of public investors to whom the information was not known constituted conduct violative of the designated antifraud provisions.<sup>26</sup>

We further concluded that by directly and indirectly effecting a series of transactions on the exchange which created active actual and apparent trading in Ramer stock and which raised the price of such stock for the purpose of inducing purchases by others, Mates engaged in conduct which constituted a manipulation of securities prices in violation of Section 9(a)(2) of the Exchange Act.

#### CONCLUSION

In view of the foregoing, we concluded that it was in the public interest to accept the offer of settlement and to impose the sanctions permitted under such offer, as recommended by our staff.

By the Commission (Chairman BUDGE and Commissioners OWENS, SMITH and NEEDHAM), Commissioner HERLONG not participating.

<sup>24</sup> Following public disclosure of the information on April 16, 1968 the price of the stock generally rose from 7<sup>1</sup>/<sub>8</sub> on that date to 13<sup>1</sup>/<sub>8</sub> on April 29, 1968.

<sup>25</sup> *Merrill Lynch, Pierce, Fenner & Smith, Inc.*; 43 S.E.C. 933, 936 (1968); See also *Blyth & Co.*, 43 S.E.C. 1037 (1969); *Van Alstyne, Noel & Co.*, 43 S.E.C. 1080 (1969).

<sup>26</sup> *S.E.C. v. Texas Gulf Sulphur Co.*, 401 F.2d 833 (C.A. 2, 1968), cert. denied, 394 U.S. 976 (1969); *Cady, Roberts & Co.*, 40 S.E.C. 907 (1961); *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, supra; *Blyth & Co.*, supra; *Van Alstyne, Noel & Co.*, supra.