

ADMINISTRATIVE PROCEEDING  
FILE NO. 3-6831

UNITED STATES OF AMERICA  
Before the  
SECURITIES AND EXCHANGE COMMISSION

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In the Matter of :  
EDWARD MICHAEL FURLONG :

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INITIAL DECISION

March 9, 1988  
Washington, D.C.

David J. Markun  
Administrative Law Judge

UNITED STATES OF AMERICA  
Before the  
SECURITIES AND EXCHANGE COMMISSION

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In the Matter of :  
EDWARD MICHAEL FURLONG : INITIAL DECISION  
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APPEARANCES: Robert D. LaFramenta, John C. Koutsos,  
and Peter A. Burke, Esqs., Los Angeles  
Regional Office, for the Division of  
Enforcement.

Respondent Edward Michael Furlong, pro  
se.

BEFORE: David J. Markun, Administrative Law Judge.

I. THE PROCEEDING

This public proceeding was instituted by an order of the Commission dated April 14, 1987 ("Order") pursuant to Sections 15(b) and 19(h) of the Securities Exchange Act of 1934 ("Exchange Act") <sup>1/</sup> to determine: (a) whether the Respondent, Edward Michael Furlong ("Furlong" or "Respondent"), was, as alleged by the Division of Enforcement ("Division") in the Order, found guilty on October 20, 1986, upon his plea of guilty, of securities fraud in violation of 15 U.S.C. §78j(b), Section 10(b) of the Exchange Act, based upon his participation in a scheme to fraudulently manipulate the share price of the common stock of Abex, Ltd.; (b) whether Respondent has any defense to the allegations, and (c) the remedial action, if any, that may be appropriate in the public interest under Sections 15(b) and 19(h) of the Exchange Act.

The evidentiary hearing was held on September 22, 1987 at the Federal Prison Camp at Boron, California. Respondent Furlong appeared pro se.

The parties have filed proposed findings of fact, conclusions of law, and supporting briefs.

The findings and conclusions herein are based upon the record. No witnesses were called. The Division relies

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1/ 15 U.S.C. §§78o(b), 78s(h).

for its proposed findings upon the entire record, including but not limited to the Order, Respondent's answer, the transcript of the hearing, and the following certified Division exhibits:

Exhibit 1:

Certified copy of the National Association of Securities Dealers, Inc. ("NASD") Board of Governors' Decision In the Matter of Edward M. Furlong barring him from association with any member of the NASD in any capacity for a period of one year;

Exhibit 2:

Certified copy of First Superceding Indictment, charging Edward Michael Furlong ("Furlong") with, inter alia, directly and indirectly, by use of the mails, knowingly and willfully, employing a manipulative scheme and artifice to defraud and engaging in acts, practices and courses of business that operated as a fraud and deceit, in connection with the purchase and sale of securities, in violation of 15 U.S.C. §78j(b), 78ff; 17 C.F.R. 240.10b-5. U.S. v. E. Michael Furlong, et al., CR 85-628-R (C.D. Cal.);

Exhibit 3:

Certified copy of transcript of Furlong's plea of guilty entered on July 11, 1986, U.S. v. Michael E. Furlong (sic), CR 85-628-R (C.D. Cal.), accompanied by declaration of its authenticity and accuracy; and

Exhibit 4:

Certified copy of Judgment and Probation/Commitment Order of Michael E. Furlong (sic.), CR 85-628-R (C.D. Cal.), entered October 20, 1986.

The standard of proof applied is that requiring proof by a preponderance of the evidence. <sup>2/</sup>

II. FINDINGS OF FACT AND LAW

Section 15(b)(6) of the Exchange Act, 15 U.S.C. §78o(b)(6), empowers the Commission, after notice and opportunity for hearing, to bar and/or to impose lesser sanctions upon any person associated with a broker or dealer when such person has been convicted of any offense specified in Section 15(b)(4)(B) of the Exchange Act, 15 U.S.C. §78o(b)(4)(B), within ten years of the commencement of the proceedings.

The Order herein, as already noted, alleges that on October 20, 1986, Respondent Furlong was convicted of having violated Section 10(b) of the Exchange Act, 15 U.S.C. §78j(b), within the period July 1983 to July 1985. Section 10(b) is among the securities laws embraced by Section 15(b)(4)(B), which covers, among other offenses, a felony that:

- (i) involves the purchase or sale of any security, or
- (ii) arises out of the conduct of the business of a broker or dealer.

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<sup>2/</sup> Steadman v. S.E.C., 450 U.S. 91, 101 S.Ct. 999 (1981).

Division Exhibits 2 through 4 establish that Respondent Furlong was indeed convicted, on October 20, 1986, on his plea of guilty, of having violated, in 1983 and 1984, Section 10(b) of the Exchange Act by participating in a fraudulent scheme to manipulate the price of Abex, Ltd. common stock while Respondent was employed by, and functioning as a registered representative of, a registered broker dealer. He was sentenced to 6 years imprisonment, 18 months to be served, followed by a period of probation. Accordingly, Respondent is subject to the imposition of an appropriate sanction if one is found to be in the public interest.

### III. THE PUBLIC INTEREST

In determining what sanction, if any, it is appropriate to apply in the public interest, it is necessary for the Commission, among other factors, to ". . . weigh the effect of . . . action or inaction on the welfare of investors as a class and on standards of conduct in the securities business generally. <sup>3/</sup> Besides serving as a

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<sup>3/</sup> Arthur Lipper Corporation, Securities Exchange Act Release No. 11773 (October 24, 1975) 8 SEC DOCKET 273, 281. Although the reviewing Court in Arthur Lipper Corp. v. S.E.C., 547 F.2d 171, 184-5 (2d Cir. 1976) reduced the Commission's sanctions on its views of facts, it recognized that deterrence of others from violation is a legitimate purpose in the imposition of sanctions.

general deterrent to dissuade others from the type of misconduct a respondent may be guilty of, a sanction must be designed to protect the public interest by providing reasonable assurance that the particular respondent being sanctioned will not himself commit the same or similar violations in the future.<sup>4/</sup> In considering the likelihood or probability of future violations by a defendant, in civil injunctive litigation, the courts assess the totality of the circumstances surrounding the defendant and his violation, looking to factors such as the degree of scienter involved, the isolated or recurrent nature of the violation, defendant's recognition of, or failure to recognize, the wrongful nature of his conduct, the sincerity of his assurances against future violations, and the likelihood, because of the defendant's professional occupation, that future violations might occur.<sup>5/</sup>

The nature of the fraudulent manipulation of the common stock of Abex, and Furlong's participation in that scheme, can perhaps best be detailed by setting forth the relevant portions of the first superseding indictment (Division Exhibit 2) to which Furlong entered a guilty plea:

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4/ In the Matter of Lester Kuznetz, Exchange Act Release No. 23525, August 12, 1986 (A.P. 3-6356), 36 SEC DOCKET 466, 470.

5/ Cf. S.E.C. v. Murphy, 626 F.2d 633, 655 (9th Cir. 1980), and cases there cited.

UNITED STATES DISTRICT COURT  
FOR THE CENTRAL DISTRICT OF CALIFORNIA  
June 1985  
Grand Jury

UNITED STATES OF AMERICA ) NO. CR 85-628  
Plaintiff ) FIRST SUPERSEDING  
v. ) I N D I C T M E N T  
LEE SHROUT ) [15 U.S.C. §§78j(b),  
RALPH ERNSTSEN, ) 78ff, 17 C.F.R.  
E. MICHAEL FURLONG, ) \$240.10b-5: Fraud in  
Defendants. ) the Purchase and Sale  
of a Security; 18 U.S.C.  
\$1341: Mail Fraud]

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The Grand Jury charges:

COUNTS ONE THROUGH SEVEN

[15 U.S.C. §§78j(b), 78ff, 17 C.F.R. \$240.10b-5]

A. INTRODUCTION

At all relevant times:

1. Abex, Ltd. ("Abex"), was a shell corporation incorporated in the state of Nevada on June 17, 1981. Shares of Abex stock were publicly traded on the Over-the-Counter (OTC) Market.

2. Defendant LEE SHROUT was the president of Corporate Registrar and Transfer, a stock transfer company, located in Newport Beach, California. Defendant SHROUT owned and controlled, directly and indirectly, various corporations, including Abex, Pacific Mortgage and Corporate Registrar and Transfer.

3. Defendant RALPH ERNSTSEN owned and controlled, directly and indirectly, various corporations, including Western Investments, Inc., Ralph and Carol Ingram, Inc., and Mountain States, Ltd.

4. Union Securities was a broker-dealer of securities, with its principal place of business in Pasadena, California.

5. Defendant E. MICHAEL FURLONG was a stockbroker employed by Union Securities.

6. Wedbush, Nobel, Cooke, Inc., ("Wedbush") was a full-service broker-dealer of securities, with its principal place of business in Los Angeles, California. Wedbush provided brokerage services to Union Securities, including the confirmation and clearance of securities transactions effected by Union Securities on behalf of its clients.

B. FRAUDULENT ACTIVITY

7. On or about a date unknown to the Grand Jury and continuing through at least January of 1984, in Los Angeles County, within the Central District of California, and elsewhere, defendants LEE SHROUT, RALPH ERNSTSEN and E. MICHAEL FURLONG and others known and unknown to the Grand Jury devised, intended to devise and employed a scheme and artifice to defraud and engaged in acts, practices and a course of business which operated as a fraud and deceit in connection with the purchase and sale of securities of Abex.

8. The scheme and artifice to defraud and the acts, practices and course of business which operated as a fraud and deceit consisted of the manipulation of the market for securities of Abex through a series of manipulative and deceptive devices.

9. The fraudulent scheme to manipulate the market for Abex stock included, but was not limited to, the following:

a. To restrict the supply of Abex stock available to be purchased and sold through the OTC market, defendant LEE SHROUT caused a one for ten reverse split of Abex stock.

b. To create interest in Abex stock and to acquire additional shares of Abex stock for himself, defendant LEE SHROUT caused Abex to issue additional stock to acquire companies owned, in whole and in part, directly and indirectly, by defendant SHROUT.

c. To create the appearance of business activity, defendant LEE SHROUT negotiated for Abex to acquire companies which required additional capital in order to operate.

d. As part of these negotiations, defendant LEE SHROUT represented that Abex would provide financial assistance to these companies, even though Abex did not have sufficient funds available to assist these companies as defendant SHROUT well knew.

e. To generate capital for Abex to acquire and operate these companies, defendant LEE SHROUT caused Abex to issue an additional one million shares of stock to be sold through a private placement in South America by Europea Consolidata.

f. The price of the Abex stock to be sold in South America by Europea Consolidata was based upon the price of Abex stock in the OTC market.

- g. To generate trading activity in Abex stock in the OTC market, defendants LEE SHROUT, RALPH ERNSTSEN and E. MICHAEL FURLONG opened or caused others to open accounts to buy and sell Abex stock.
- h. Defendant LEE SHROUT caused accounts to be opened by Pacific Mortgage at Union Securities and at C. L. McKinney, a broker-dealer located in Los Angeles, California.
- i. Defendant RALPH ERNSTSEN caused accounts to be opened at Union Securities by Western Investments, Inc., Mountain States, Ltd., and Ralph and Carol Ingram, Inc.
- j. Defendant RALPH ERNSTSEN directed Margaret Bossick to open an account at Union Securities and to act as a nominee for defendant ERNSTSEN.
- k. Defendant E. MICHAEL FURLONG opened accounts at Union Securities in the names of relatives and in the names of individuals employed by or associated with defendant LEE SHROUT.
- l. To generate trading activity and increase the price of Abex stock, defendants LEE SHROUT, RALPH ERNSTSEN and E. MICHAEL FURLONG placed, or caused others to place orders to purchase Abex stock through Union Securities.
- m. To control the supply of the Abex stock and to prevent the price of the stock from decreasing, defendant E. MICHAEL FURLONG purchased Abex stock offered for sale in the OTC market and placed the stock in accounts that had been established by the defendants at Union Securities. In addition, defendant E. MICHAEL FURLONG purchased Abex stock for clients of Union Securities without first receiving the required authorization from the clients.
- n. To induce Wedbush to extend the time in which clients of Union Securities had to pay for purchases of Abex stock, defendant E. MICHAEL FURLONG falsely represented to Wedbush that the clients would pay for the purchases when he knew that the clients did not have the ability or intention to pay for the purchases.
- o. To create the appearance of activity in Abex stock and to prevent the liquidation of accounts at Union Securities by Wedbush, defendant E. MICHAEL FURLONG simultaneously purchased and sold Abex stock for accounts at Union Securities. To accomplish these matched trades, defendant E. MICHAEL FURLONG sold Abex stock to stock traders and thereafter repurchased the stock from the stock traders for different accounts.

p. To create interest in Abex stock, defendant LEE SHROUT caused misleading articles regarding the business plans and activity of Abex to be published in stock journals and publications.

q. To create interest in Abex and to convince investors to purchase shares of Abex stock, defendant LEE SHROUT caused the preparation and dissemination of corporate reports containing false and misleading financial information.

\* \* \*

t. As a result of the manipulation of Abex stock by the defendants, the price of Abex stock increased from less than \$.10 per share in August, 1983 to over \$5.00 per share in January, 1984.

C. PURCHASE OF SECURITY

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COUNTS FIFTEEN THROUGH EIGHTEEN  
[15 U.S.C. §§78j(b), 78ff, 17 C.F.R.  
§240.10b-5]

1. The Grand Jury repeats and realleges each and every allegation in paragraphs One through Nine of Counts One through Seven of this Indictment as though set forth herein as constituting the defendants' manipulative scheme and artifice to defraud and acts practices and course of business that operated as a fraud and deceit in connection with the purchase and sale of Abex stock.

2. On or about the dates listed below, in Los Angeles County, within the Central District of California, and elsewhere, defendants RALPH ERNSTSEN and E. MICHAEL FURLONG, directly and indirectly, by the use of the mails, knowingly and willfully employed the above-described manipulative scheme and artifice to defraud and engaged in the above-described acts, practices and course of business that operated as a fraud and deceit in that the defendants caused confirmations to be mailed from Wedbush in connection with the following purchases or sales of Abex stock:

<u>COUNT</u>	<u>DATE OF MAILING</u>	<u>ADDRESSEE</u>	<u>NUMBER OF SHARES</u>	<u>PRICE</u>
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Seventeen	12/27/83	Ralph Ingram and Carol Ingram, Inc. (sale) 1605 E. Charleston Blvd., Apt. 4 Las Vegas, Nevada	8500	\$39,950
Eighteen	1/05/84	Mountain States, Ltd. 1605 E. Charleston Blvd. Las Vegas, Nevada	10,000	\$84,750 (sale)

As already noted, Respondent Furlong pleaded guilty to the charges of having violated Section 10(b) of the Exchange Act, as set forth above. He was represented by assigned counsel at the time, and the United States District Judge, as shown by Exhibit 3, carefully and extensively examined Furlong to ensure that his guilty plea was entered knowingly and without any duress or improper promises and in full knowledge of the range of punishment to which his guilty plea subjected him.

Violation of Section 10(b) of the Exchange Act necessarily involves the element of scienter. <sup>6/</sup>

That the sentencing Judge considered this an egregious case of stock manipulation on the part of defendant Furlong seems evident from the substantial sentence that was imposed, i.e. 6 years imprisonment, 18 months to be served, 54 months suspended, with 5 years probation to commence upon release from confinement. This was the

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<sup>6/</sup> Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976);  
Aaron v. S.E.C., 446 U.S. 680 (1980).

sentence imposed notwithstanding the lack of prior convictions and notwithstanding its imposition on the basis of a plea rather than after trial.

Respondent argues that he has been in the securities industry for 33 years <sup>7/</sup> and that the Abex stock manipulation is his first offense. Unfortunately, this circumstance cuts both ways, since while it is to his credit that he has no prior violations, his lengthy experience should have taught him without the least bit of doubt that stock manipulation is a very serious violation indeed, and one that very frequently results in being barred from the securities business.

Stock manipulations can have serious side effects on the business of broker dealer firms, as was the case here.

On January 31, 1984, Furlong's employer, Union Securities, notified the Commission and the National Association of Securities Dealers ("NASD") that it had suspended Furlong pending resolution of the firm's net capital problem, which was caused by Furlong's opening customer accounts that purchased stock of Abex, Ltd. and later failed to pay debit balances when required at

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<sup>7/</sup> Respondent Furlong chose not to testify at the hearing, with the result that a number of facts he "argues" are not established in the record; however, I am here assuming that his stated years in the securities business and his lack of prior violations are correct.

settlement date or after extension date.

Subsequently, due to his failure to cooperate with the NASD in its inquiry into events surrounding the scheme to raise the price of Abex Ltd. common stock, the NASD on September 30, 1985, barred Furlong from association with any member firm for a period of one year.

Respondent Furlong's arguments demonstrate very little awareness on his part of the seriousness of his violation and offer little by way of assurance against future violations were he allowed to continue in the securities business. Thus, he argues in his brief: <sup>8/</sup>

. . . . He [Furlong] feels he was the 'scape-goat' or 'fall guy' of the Abex fiasco. He personally felt Abex was a good speculative situation until early January, 1984. He was not alone, as the facts of the case will attest. He ended up being a victim, certainly not an instigator. He received no stock, options fees or monies. His only source of income from Abex was the commissions he received. He charged only regular commissions and reduced rates on the larger trades. He always traded as near the bid as possible. He thereafter protected the capital of the investors, and was not guilty of personally influencing the rise or fall in the price of Abex stock as charged.

What the Commission said in In the Matter of Lester Kuznetz, (cited in footnote 4 above), at 36 SEC DOCKET 470, applies with equal force to Respondent Furlong on the basis

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<sup>8/</sup> As noted in footnote 7 above, Furlong elected not to testify at the hearing, nor did he attempt to adduce any other evidence.

of the record in this proceeding:

[Respondent's] misconduct was egregious. Despite his many years of experience, he demonstrated a total lack of sensitivity to the obligation of fair dealing borne by those who engage in the securities business. In an industry that presents so many opportunities for abuse and over-reaching and depends so heavily on the integrity of its participants, such behavior cannot be countenanced. [Respondent's] actions support his permanent exclusion from the securities business.

We recognize the serious effect of the sanction we are imposing. However, the sanction is designed to protect the public interest by preventing [Respondent] from again engaging in such fraudulent activity. At the same time, it serves the purpose of general deterrence and should act as a warning to any other participant in the securities industry who might be tempted to engage in similar misconduct. [Footnote omitted] In light of the circumstances, we are convinced that the public interest requires [Respondent's] unqualified bar from association with any broker dealer.

All arguments of the Respondent have been carefully considered. As already noted, he claims he was a "scape-goat" or "fall guy" in the Abex manipulation, and claims he was poorly advised by (assigned) counsel when he pleaded guilty. Furlong says he is appealing his conviction. Meanwhile, however, the sanction herein must be predicated upon his conviction on his guilty plea. Should Respondent be successful in reversing his criminal conviction, he would of course be free to apply to the Commission for appropriate relief from any Commission sanction imposed in this proceeding. Furlong does not suggest what sanction might be appropriate. His arguments in denial or in

mitigation are not supported by evidence (as already noted above, he chose not to testify or offer other evidence), and I do not find them persuasive.

The Division urges strongly that only a permanent bar will adequately protect the public from a recurrence of misconduct on Respondent's part and also deter other potential violators. I concur in the view that a permanent bar, both for remedial and deterrent purposes, is appropriate and necessary in the public interest.

#### IV. ORDER

Accordingly, IT IS ORDERED that Respondent Edward Michael Furlong is hereby barred from association with a broker or dealer. <sup>9/</sup>

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

Pursuant to Rule 17(f), this initial decision shall become the final decision of the Commission as to each

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<sup>9/</sup> The Division urges that Furlong be barred from association with any broker, dealer, investment adviser, investment company, or municipal securities dealer under the Commission's authority to "place limitations" on regulated entities and persons. No authority is cited for this proposition, other than "settled" cases. I conclude that the "place limitations" language cannot be given such an expansive application, however desirable and practical that result might be in particular cases.

party who has not, within fifteen (15) days after service of this initial decision upon him, filed a petition for review of this initial decision pursuant to Rule 17(b), unless the Commission pursuant to Rule 17(c) determines on its own initiative to review this initial decision as to him. If a party timely files a petition for review, or the Commission takes action to review as to a party, the initial decision shall not become final with respect to that party. <sup>10/</sup>

  
David J. Markun  
Administrative Law Judge

Washington, D.C.  
March 9, 1988

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<sup>10/</sup> All proposed findings, conclusions and supporting arguments have been considered. To the extent that the proposed findings and conclusions submitted are in accordance with the findings, conclusions and views stated herein they have been accepted, and to the extent they are inconsistent therewith they have been rejected. Certain proposed findings and conclusions have been omitted as not relevant or as not necessary to a proper determination of the material issues presented.