SECURITIES AND EXCHANGE COMMISSION
Washington, D.C.

SECURITIES ACT OF 1933
Rel. No. 8888 / January 31, 2008

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 57246 / January 31, 2008

Admin. Proc. File No. 3-11626

In the Matter of

JOHN A. CARLEY,
EUGENE C. GEIGER,
THOMAS A. KAUFMANN,
EDWARD H. PRICE, and
CHRISTOPHER H. ZACHARIAS

OPINION OF THE COMMISSION

BROKER-DEALER PROCEEDING

CEASE-AND-DESIST PROCEEDING

Grounds for Remedial Action

Unregistered Offer and Sale of Securities

Fraud

Failure to Report Securities Transactions

Failure to Supervise

Officers of issuer unlawfully made unregistered offers and sales of securities. Officers committed fraud by omitting to disclose material facts concerning the sale of unregistered securities. One of the officers also failed to report a securities transaction. Held, it is in the public interest to order officers to disgorge ill-gotten profits and to cease and desist from committing or causing any violations or future violations of Sections 5(a), 5(c), and 17(a) of the Securities Act of 1933, Sections 10(b) and 13(a) of the Securities Exchange Act of 1934, and Exchange Act Rules 10b-5, 12b-20, 13a-1, and 13a-11.

Associated persons of broker-dealer made unregistered offers and sales of securities. Held, it is in the public interest to order associated persons to disgorge ill-gotten profits; to pay civil money penalties, to cease and desist from committing or causing any violations or future violations of Securities Act Sections 5(a) and 5(c); to bar one associated person from association with a broker or dealer and to bar the other associated person from association with a broker or dealer with a right to reapply after five years.

President, chief executive officer, and chief compliance officer of registered broker-dealer failed to exercise reasonable supervision over associated persons with a view to preventing their violations of the securities laws. Held, it is in the public interest to bar president, chief executive officer, and chief compliance officer from association with any broker or dealer in a supervisory capacity and to order him to pay a civil money penalty.

APPEARANCES:

Thomas D. Birge and Carla B. Minckley, of Birge & Minckley, P.C., for John A. Carley.

Bradford J. Lam, of the Law Offices of Bradford J. Lam, PLLC, for Eugene C. Geiger.

Jeffrey J. Scott, of Scott & Associates, P.C., for Thomas A. Kaufmann.

Gordon Dihle, for Edward H. Price.

David A. Zisser, of Isaacson Rosenbaum, P.C., for Christopher H. Zacharias.

Julie K. Lutz and Thomas J. Krysa, for the Division of Enforcement.

Appeal filed: August 5, 2005
Last brief received: December 28, 2005
Oral argument: February 7, 2007

I.

Respondents John A. Carley, Eugene C. Geiger, Thomas A. Kaufmann, Edward H. Price, and Christopher H. Zacharias each appeal from the decision of an administrative law judge. Carley and Zacharias were officers and directors of Starnet Communications International, Inc. ("Starnet"), a Delaware corporation with its principal places of business in St. Johns, Antigua and Vancouver, British Columbia, Canada. 1/ Geiger and Kaufmann were associated persons of Spencer Edwards, Inc. ("Spencer Edwards"), a registered broker-dealer. Price was president, chief executive officer, and chief compliance officer of Spencer Edwards; he supervised Geiger and Kaufmann. The law judge found that Carley and Zacharias violated, and Geiger and Kaufmann willfully violated, Sections 5(a) and 5(c) of the Securities Act of 1933 2/ by offering to sell, selling, and delivering to members of the public shares of Starnet common stock when no registration statement was filed or in effect with respect to those securities and no exemption from registration was available. The law judge found that Price failed reasonably to supervise Geiger and Kaufmann. 3/ The law judge also found that Carley and Zacharias violated the antifraud provisions of the federal securities laws by filing current and annual reports with the Commission that were false and misleading. 4/ The law judge further concluded that Zacharias violated Section 16(a) of the Securities Exchange Act of 1934 and Exchange Act Rule 16a-3 5/ by failing to file a required Form 4.

The law judge imposed cease-and-desist orders on Carley, Zacharias, Geiger, and Kaufmann, barred Geiger and Kaufmann from associating with any broker or dealer, and barred Price from associating with any broker or dealer in a supervisory capacity. The law judge ordered Carley and Zacharias each to disgorge an amount representing payments made to them in connection with their unregistered sale of shares of Starnet common stock. The law judge ordered Geiger and Kaufmann each to disgorge fifty percent of the net commissions that they earned on all Starnet trades attributable to their joint account number at Spencer Edwards from January 1999 through February 2001. The law judge imposed third-tier penalties of $400,000

1/ On May 25, 2001, Starnet became a wholly-owned subsidiary of World Gaming PLC, a company organized in England and Wales.

2/ 15 U.S.C. §§ 77e(a), 77e(c).

3/ The law judge also found that Spencer Edwards failed reasonably to supervise Geiger and Kaufmann. Spencer Edwards did not appeal, and we declared the law judge's decision final. Roy E. Gould, Securities Act Rel. No. 8603 (Aug. 18, 2005), 86 SEC Docket 94, 95.

4/ 15 U.S.C. §§ 77q(a), 78j(b); 17 C.F.R. § 240.10b-5.

5/ 15 U.S.C. § 78p(a); 17 C.F.R. § 240.16a-3.

against Geiger and $300,000 against Kaufmann. He imposed a second-tier penalty of $150,000 against Price.

We base our findings on an independent review of the record except with respect to those findings not challenged on appeal.

II.

This case arises from a complex series of transactions involving the unregistered offer and sale of Starnet stock to the public. Officers of Starnet together with associated persons of a broker-dealer engaged in a distribution of Starnet shares to the public without registration or exemption from registration in violation of the federal securities laws. The violative distribution was designed to enable Starnet's officers, directors, and employees to sell and receive the proceeds from sales of stock received upon exercise of employee stock options. Seven foreign entities, which were controlled by a single adviser and which held Starnet common stock and warrants, previously acquired in unregistered transactions, participated in the illegal distribution.

The Starnet officers compounded the foregoing violations by omitting to disclose material facts concerning the nature of the related party transactions involving the exercise of employee stock options by Carley and Zacharias. One of the officers also violated the reporting provisions by failing to report his acquisition of Starnet shares. Finally, the broker-dealer's president failed to exercise reasonable supervision over the associated persons.

In Part III, we discuss the "swap" transactions that resulted in the unregistered distribution of Starnet stock to the public in connection with the exercise of employee stock options. Part IV considers whether the offers and sales of Starnet stock violated the registration requirements of the securities laws and discusses the Respondents' arguments with respect to the availability of the safe harbors provided by Regulation S and Securities Act Rule 144, as well as the exemptions from registration provided in Securities Act Section 4. In Part V, we describe the steps taken by the president of the broker-dealer to supervise the two associated persons and address the adequacy of that supervision. In Part VI, we consider the omissions in Starnet's public filings that form the basis for the fraud allegations against the two Starnet officers. Part VII addresses the alleged Exchange Act Section 16 reporting violation. In Part VIII, we address the Respondents' procedural arguments concerning severance and the statute of limitations. Part IX concludes with an analysis of what sanctions are appropriate in the public interest.

III.

In Section A below, we discuss the "swap" transactions that resulted in the unregistered distribution of Starnet stock to the public. In Section B, we discuss the role played by each Respondent in those transactions.

A. From September 1997 until May 2001, Starnet common stock traded on the OTC Bulletin Board and was registered with the Commission pursuant to Section 12(g) of the Exchange Act. 6/ In the late 1990s, Starnet created two employee stock option plans as incentive compensation for its officers, directors, and employees ("Option Holders"). Starnet filed its first Form S-8 with the Commission on March 12, 1998 to register the offer and sale of 3 million shares of common stock upon exercise of employee stock options issued under Starnet's 1997 Stock Option Plan. Starnet filed its second Form S-8 with the Commission on March 10, 1999 to register the offer and sale of 4 million shares of common stock upon exercise of employee stock options issued under Starnet's 1999 Stock Option Plan. 7/ The Stock Option Plans, which were attached as exhibits to the Forms S-8, stated that the exercise of the options would be deemed effective upon payment to Starnet of the option price. The Forms S-8 did not register the resale of the Plan Shares, and Starnet never filed any post-effective amendments to its Forms S-8. 8/

Shortly after filing its first Form S-8, Starnet learned, in April 1998, from its Canadian counsel that the British Columbia securities laws would impose an indefinite holding period on any Plan Shares issued to Starnet's Canadian Option Holders. Counsel further opined that British Columbia securities laws could also limit the resale of Plan Shares in the United States resulting from the exercise of such options. 9/

In or around December 1998, Zacharias discussed with Roy E. Gould, a resident of Vancouver, British Columbia, Canada, and a partial owner of United Capital Securities, Inc. ("United Capital"), a Canadian broker-dealer, the limitations under the British Columbia securities laws on the resale of Starnet shares issued upon exercise of stock options. 10/ Gould

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6/ 15 U.S.C. § 78*l*(g).

7/ The shares of common stock issued upon the exercise of options issued under the 1997 and 1999 Stock Option Plans hereinafter are referred to as "Plan Shares."

8/ Form S-8 provides, in certain situations, for the resale of shares pursuant to a reoffer prospectus or a post-effective amendment to the Form. See General Instruction C to Form S-8, Fed. Sec. L. Rep. (CCH) ¶ 8141.

9/ Canadian counsel suggested that the options be issued to a trust account directed by a non-Canadian trustee. Starnet, however, decided not to create such a trust. See infra note 56.

10/ In late 1998 and 1999, Starnet's stock price began to rise as it shifted its business operations from adult entertainment to Internet gambling. Between June and December 1998, Starnet stock traded at prices between $0.37 and $1.50 per share. By early July 1999, Starnet's stock traded at prices above $26 per share, and its daily trading volume

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contacted Kaufmann at Spencer Edwards, and Starnet's chief executive officer, Mark N. Dohlen, contacted Geiger at Spencer Edwards. Geiger's long-time client, Alfred Peeper, controlled seven foreign entities (the "Peeper Entities") that had acquired common stock (the "1997 Shares"), warrants, and piggyback warrants from Starnet in an unregistered offering pursuant to Regulation S in December 1997. 11/ Gould and Dohlen asked whether the Peeper Entities would "swap" their Starnet common stock for Plan Shares issued to Starnet's Option Holders. Peeper agreed. Zacharias, Geiger, Kaufmann, Gould, and Peeper subsequently developed a procedure involving sales to the public of the Peeper Entities' Starnet common stock, followed by offsetting transfers of Starnet Plan Shares to the Peeper Entities. 12/ In this manner, Starnet's Option Holders would receive the financial benefit equivalent to both the "cashless" exercise of their options and the subsequent sale of the shares obtained upon exercise into the open market. 13/

10/ (...continued)
exceeded 1.5 million shares. As a result, Starnet's Canadian Option Holders wanted to exercise their options and sell the resulting Plan Shares.

11/ On December 2, 1997, Starnet issued 2.45 million shares of common stock, with warrants, to the Peeper Entities, in consideration for $2.45 million. As reported in its Form 8-K filed on December 11, 1997, Starnet issued these shares in unregistered transactions pursuant to Rule 903 of Regulation S. Each of the seven Peeper Entities received 350,000 shares of common stock; warrants attached to the shares could be exercised at $2.00 per share and expired in one year. Each warrant exercised at $2.00 per share entitled the purchaser to one share of common stock and a second warrant, the "piggyback" warrant, which could be exercised at $4.00 per share within one year of the "piggyback" warrant being issued. In total, these warrants gave the Peeper Entities the right to purchase an additional 4.35 million shares of Starnet common stock. In addition, Starnet issued an additional two blocks of 350,000 shares to the Peeper Entities.

12/ The law judge found that Gould willfully violated Securities Act Sections 5(a) and 5(c) by offering and selling unregistered Starnet securities and that he willfully violated Exchange Act Section 15(a), 15 U.S.C. § 78o(a), by engaging in business in the United States as an unregistered broker. Gould did not appeal the initial decision of the law judge. We declared that decision final. Roy E. Gould, 86 SEC Docket at 95.

Dohlen, Peeper, and Paul A. Giles, a president and director of Starnet, were each named in the OIP but were severed from this proceeding because they had not been served with the OIP. John A. Carley, Securities Exchange Act Rel. No. 50954 (Jan. 3, 2005), 84 SEC Docket 2317. Our findings with respect to Dohlen, Peeper, and Giles are solely for the purpose of this opinion.

13/ The only document to describe this arrangement in its totality is a memorandum by Dennis Brovarone, Peeper's attorney, dated September 29, 1999 and addressed to

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To implement this procedure, Starnet required its Option Holders to open brokerage accounts with Gould at United Capital. When these Option Holders wished to exercise their stock options, they executed an irrevocable authorization permitting Gould to exercise their options and transfer the resulting Plan Shares to one or more of the Peeper Entities' accounts. 14/ The Peeper Entities that did not previously have accounts at Spencer Edwards opened new accounts in 1999 to participate in this procedure. Geiger and Kaufmann served as account executives to all of the Peeper Entities. Gould notified Kaufmann or Geiger at Spencer Edwards of the aggregate number of shares that the Option Holder wished to sell, and then Kaufmann or Geiger would execute the sale of the equivalent number of Starnet shares to the public from the Spencer Edwards accounts of one or more of the Peeper Entities.

After payment of commissions, Spencer Edwards transmitted the net proceeds from the Peeper Entities' sales to Dennis Brovarone, Peeper's attorney. Brovarone deposited the funds in client trust accounts and then wired from the trust account a portion of the proceeds equal to the exercise price for the applicable options to Starnet. Starnet in turn issued Plan Shares in the name of the Option Holder. Consistent with the terms of the irrevocable authorization, however, the Plan Shares were delivered to Gould at United Capital. Gould sent the Plan Shares to the appropriate Peeper Entity's Spencer Edwards account as reimbursement for the shares of Starnet common stock that the Peeper Entity had sold. Upon delivery of the Plan Shares to the Peeper Entity, Brovarone wired the balance of the proceeds to the Option Holder's United Capital account. The Peeper Entities then resold the Plan Shares into the public market at a time of their choosing for their own financial benefit.

By the end of 1998 the Peeper Entities did not hold enough 1997 Shares to offset the anticipated quantities of Plan Shares to be sold by the Option Holders. By December 1998, Starnet's Option Holders held options for 3 million shares (and would soon hold options for another 4 million shares to be issued under the 1999 Stock Option Plan). In contrast, the Peeper Entities had already sold some of the 2.45 million 1997 Shares. Moreover, the warrants attached

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13/ (...continued)
Zacharias, Kaufmann, Gould, and Peeper. In addition to outlining the arrangement as described above, the memorandum stated that "[t]he Peeper accounts received ?????? for their services." This memorandum was written at Peeper's request. At the hearing, Zacharias and Gould agreed that the memorandum accurately described the manner in which the sale of the Plan Shares was implemented. None of the Respondents disputes the accuracy of the memorandum.

14/ The irrevocable authorization stated that Starnet was "facilitating this trade," that shares were being sold "on my [the Option Holder's] behalf" prior to the receipt of the Plan Shares, and that Gould would transfer the shares received in the Option Holder's name "into an appropriate account in order to reimburse for the shares sold on my behalf." The Option Holder also authorized Gould "to pay directly to Starnet the strike price per share upon the sale of the shares."

to the 1997 Shares expired on December 2, 1998, and the Peeper Entities had no incentive to exercise them at $2.00 per share when Starnet common stock was trading at about $1.00 per share at or around this time. Consequently, on December 2, 1998, Starnet extended for one year the period in which the Peeper Entities could exercise their warrants. 15/

During 1999, Starnet's stock price rose; by early July 1999, it was trading at above $26 per share, with daily trading volume in excess of 1.5 million shares. From January to October 1999, the seven Peeper Entities acquired 4.9 million shares from Starnet by exercising their warrants and piggyback warrants and deposited the shares into their Spencer Edwards accounts, where they were commingled with other shares held by the Peeper Entities, including the 1997 Shares and Plan Shares. As Starnet's Option Holders exercised their stock options during this period, the seven Peeper Entities sold shares of Starnet common stock to the public to finance these option exercises. After the Peeper Entities received the Plan Shares from the Option Holders as reimbursement, they sold those shares into the market for their own financial benefit. In total, the Peeper Entities sold more than 5.2 million shares of Starnet common stock in this distribution from January 1999 through February 2001.

B. Carley was Starnet's chairman of the board and its chief financial officer. 16/ Carley opened a brokerage account at United Capital in December 1998 to participate in the procedure to "swap" his Plan Shares with the Peeper Entities' shares. He received $2.48 million through this account in connection with his exercise of stock options and subsequent sale of the Plan Shares to the Peeper Entities between February and August 1999. Zacharias opened a brokerage account at United Capital before December 1998. He received $1.45 million through this account in connection with his exercise of stock options and subsequent sale of the Plan Shares to the Peeper Entities between February and August 1999. In connection with their participation in the procedure, both executed irrevocable authorizations permitting Gould to exercise their stock options and to transfer the Starnet shares obtained upon exercise to the Peeper Entities.

Brokerage accounts at Spencer Edwards also were opened in the names of Starnet officers, including Carley and Zacharias, as part of the plan to "swap" shares held by the Peeper Entities with Plan Shares. Carley testified that he was told this was a "control account," although he did not explain what that meant. Carley signed certain documents and a margin agreement in connection with the account. Carley received brokerage statements for the account in his name, but testified that he did not control the transactions in that account, and he did not consider himself the owner of stock in the account or entitled to any proceeds from the account. Zacharias

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15/ See Starnet's Form 8-K, filed December 17, 1998, as amended by Form 8-K/A, filed March 18, 1999. The law judge found that Starnet's decision to extend the warrant exercise period "brought the scheme to life."

16/ Carley resigned from his positions at Starnet on December 23, 1999. He remained president of EFS Caribbean, Inc., Starnet's electronic credit card subsidiary, until April 3, 2000.

testified that he also received statements for the account in his name, but claimed that he did not read any statements after the first one and did not know what stock was traded through that account. He stated that "someone" at Spencer Edwards told him that this account was "unimportant" and that it was "necessary as part of the process of exercising options" and "nothing that [he] needed to worry about." He testified further that, from his point of view, transactions conducted in that account involved someone else's money. Approximately 345,000 shares of Starnet stock were sold through accounts at Spencer Edwards in the names of Carley and Zacharias. The law judge found that neither Carley nor Zacharias received any proceeds from the trading accounts in their names at Spencer Edwards. 17/

As Starnet's secretary, treasurer, and corporate counsel, Zacharias participated in establishing Starnet's stock option plans and served as a liaison with Starnet's outside counsel. 18/ Zacharias reviewed the 1998 Form S-8 and drafted the 1999 Form S-8.

Kaufmann and Geiger were the account executives for the Peeper Entities, for the Starnet officers, including Carley and Zacharias, and for an entity called Celestine Asset Management that was controlled by Gould, and executed transactions in Starnet stock in these accounts. Kaufmann has been associated with Spencer Edwards since November 1993. At the time of the hearing before the law judge, Kaufmann was the vice president of sales, a position he had held for eight years. Geiger was associated with Spencer Edwards from November 1993 through January 31, 2001. Kaufmann and Geiger worked together at Spencer Edwards under a joint account executive number, shared a private office, and split commissions on all transactions conducted in accounts managed under their joint account executive number.

Geiger had advised Peeper to participate in Starnet's 1997 Regulation S offering and, in connection with the offering, had traveled to Vancouver twice to examine Starnet's operations on Peeper's behalf. Geiger was aware that Starnet stock obtained from the exercise of warrants and piggyback warrants was being placed in the Peeper Entities' accounts and shortly thereafter resold to the public. Geiger processed orders in Starnet stock from Peeper and then from Gould after Peeper gave Geiger written notice in December 1998 that he had authorized Gould to conduct transactions in the Peeper Entities' accounts at Spencer Edwards. 19/

17/ The record is not clear as to the precise number of Plan Shares that were transferred directly to the Peeper Entities -- versus those that were placed into Starnet officers' Spencer Edwards accounts -- to complete the "swap" for the shares held by those entities.

18/ Zacharias resigned as secretary, treasurer, and director on August 12, 1999, and resigned as corporate counsel on February 14, 2000.

19/ Geiger also was receiving valuable consideration from the Peeper Entities in the form of legal fees, housing and house-related expenses, capital gains from the sale of one of the

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Kaufmann also accepted orders from Gould directing the sale to the public of Starnet stock from the Peeper Entities' accounts. The record reflects that Gould sent Kaufmann hundreds of facsimile messages containing such orders. Kaufmann also testified that Gould would "call . . . in the morning to let us know how much stock for the employees would need to be sold." Kaufmann and Gould exchanged numerous e-mails through Kaufmann's private e-mail accounts. Along with Gould, Kaufmann kept a running total of the stock being sold by the Peeper Entities' accounts. The trading instructions that Kaufmann received from Gould with respect to the Peeper Entities' accounts usually did not refer to a specific account, indicating that the accounts were being used as a fungible pool of stock to facilitate the exercise of stock options by Starnet's officers and employees. 20/ Kaufmann also executed orders for the sale of Plan Shares from the Starnet officers' Spencer Edwards accounts. 21/

IV.

Violations of the Registration Requirements

Securities Act Section 5(a) prohibits any person, directly or indirectly, from selling a security in interstate commerce unless a registration statement is in effect as to the offer and sale of that security or there is an applicable exemption from the registration requirements. Securities Act Section 5(c) prohibits the offer or sale of a security unless a registration statement as to such security has been filed with the Commission, or an exemption is available. 22/ The purpose of

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19/ (...continued)
houses that he lived in without paying rent or a mortgage, and a country club membership.

20/ In a facsimile dated April 6, 1999, that Gould sent Brovarone, Gould stated that "it doesn't really matter which account [the shares] come[] from as long as the amounts are correct." In a facsimile dated April 15, 1999, from Gould to Brovarone, Gould instructed that "if insufficient funds are in the accounts request them from Tom [Kaufmann] or take them from another account as it should all balance out in the end."

21/ Kaufmann completed Forms 144 for the Starnet stock sales associated with the accounts of Carley and Zacharias. Certain forms misstated the number of outstanding shares of Starnet, and none of the Forms 144 for the transactions was filed with the Commission.

22/ 15 U.S.C. § 77e(a) and (c); see also Jacob Wonsover, 54 S.E.C. 1, 8 (1999), petition denied, 205 F.3d 408 (D.C. Cir. 2000); Michael A. Niebuhr, 52 S.E.C. 546, 549 (1995).

the registration requirements is to "protect investors by promoting full disclosure of information thought necessary to informed investment decisions." 23/

The elements of a prima facie violation of Section 5 are that (1) no registration statement was filed or in effect as to the security; (2) the respondents, directly or indirectly, sold or offered to sell the security; and (3) interstate transportation or communication or the mails were used in connection with the offer or sale. 24/ A showing of scienter is not required to establish a violation of Section 5. 25/

It is undisputed that the stock sales at issue here were not registered under the Securities Act. The Respondents argue that these sales need not have been registered because at least one of several possible exemptions from registration applies to each sale at issue. Exemptions from registration are affirmative defenses that must be established by the person claiming the exemption. 26/ Further, "exemptions from the general policy of the Securities Act requiring registration are strictly construed against the claimant." 27/ Evidence in support of an exemption must be explicit, exact, and not built on mere conclusory statements. 28/

In support of their exemption claims, Respondents attempt to isolate certain components of the distribution and argue that various exemptions to registration apply to those component transactions. However, the registration requirements of the Securities Act apply to the "entire process in a public offering through which a block of securities is dispersed and ultimately comes

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23/ SEC v. Ralston Purina Co., 346 U.S. 119, 124 (1953); SEC v. Murphy, 626 F.2d 633, 642-43 (9th Cir. 1980).

24/ SEC v. Cont'l Tobacco Co., 463 F.2d 137, 155 (5th Cir. 1972).

25/ Swenson v. Engelstad, 626 F.2d 421, 424 (5th Cir. 1980) ("The Securities Act of 1933 imposes strict liability on offerors and sellers of unregistered securities . . . regardless of . . . any degree of fault, negligent or intentional, on the seller's part.") (internal citation omitted); SEC v. Universal Major Indus. Corp., 546 F.2d 1044, 1046-47 (2d Cir. 1976).

26/ Engelstad, 626 F.2d at 425; Lively v. Hirschfeld, 440 F.2d 631, 632 (10th Cir. 1971).

27/ Gearhart & Otis, Inc., 42 S.E.C. 1, 4-5 n.3 (1964) (citing Ralston Purina, 346 U.S. 119 (1953)), aff'd, 348 F.2d 798 (D.C. Cir. 1965); see also Murphy, 626 F.2d at 641; Quinn & Co. v. SEC, 452 F.2d 943, 945-46 (10th Cir. 1971).

28/ Robert G. Weeks, Exchange Act Rel. No. 48684 (Oct. 23, 2003), 81 SEC Docket 1319, 1337 n.35; V.F. Minton Sec., Inc., 51 S.E.C. 346, 352 (1993) (and authority cited therein), aff'd, 18 F.3d 937 (5th Cir. 1994) (Table).

to rest in the hands of the public." 29/ Here, the record shows that, beginning in January 1999, the sales of Starnet stock at issue were effectuated as part of a single, ongoing distribution of unregistered Starnet stock from Starnet to the public. We address Respondents' arguments with respect to each exemption below.

1. Possible Exemptions From Registration

a. Securities Act Section 4(1)

Securities Act Section 4(1) exempts from the registration requirement "transactions by any person other than an issuer, underwriter, or dealer." The term "underwriter" is defined to mean "any person who has purchased from an issuer with a view to, or offers or sells for an issuer in connection with, the distribution of any security . . . ." 30/

Section 4(1) is intended to exempt routine trading transactions between individual investors with respect to securities already issued and not to exempt distributions by issuers or acts of other individuals who engage in steps necessary to such distributions. 31/ Individual investors who are not securities professionals may be deemed "underwriters" within the statutory meaning of that term if they act as links in a chain of securities transactions from issuers or control persons to the public. 32/ A sale by the intermediary in such a distribution is a transaction by an underwriter and thus not exempt from registration under Section 4(1).

(i) Sales by the Peeper Entities. Zacharias and Geiger each argue that the exemption provided by Section 4(1) applies to the resale of the 2.45 million 1997 Starnet Shares originally issued to the Peeper Entities pursuant to Regulation S. 33/ Kaufmann and Geiger maintain that,

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29/ Wonsover, 54 S.E.C. at 13 n.25.

30/ Securities Act Section 2(11), 15 U.S.C. § 77b(a)(11).

31/ See Preliminary Note to Rule 144, 17 C.F.R. § 230.144; Owen V. Kane, 48 S.E.C. 617, 619 (1986), aff'd, 842 F.2d 194 (8th Cir. 1988).

32/ See Preliminary Note to Rule 144, 17 C.F.R. § 230.144; Quinn & Co., Inc., 44 S.E.C. 461, 464 (1971), aff'd, 452 F.2d 943 (10th Cir. 1971); see also SEC v. Holschuh, 694 F.2d 130, 138 (7th Cir. 1982) (stating that "even assuming that a particular defendant is not an issuer, underwriter, or dealer, he is not protected by Section 4(1) if the offer or sale of unregistered securities in question was part of a transaction by someone who was an issuer, underwriter, or dealer").

33/ Geiger also suggests that the resales of the Regulation S stock were exempt under Rule 904 of Regulation S. 17 C.F.R. § 230.904. However, two general conditions apply to all

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because the Peeper Entities purchased these shares in December 1997, the stock had come to rest under Regulation S and could be sold by the Peeper Entities in 1999 without restriction pursuant to Section 4(1).

Beginning in January 1999, the Peeper Entities purchased shares from Starnet through the exercise of warrants and piggyback warrants with a view to reselling those shares to the public, commingled those shares with the 1997 Shares, and then resold the shares of Starnet common stock (including the 1997 Shares) to the public in order to fund the option exercises of Starnet Option Holders. Starnet extended the term of the warrants for one year to enable the Peeper Entities to function as a conduit for the sale of Plan Shares and other shares of Starnet common stock to the public without registration. Once a Starnet Option Holder determined to exercise his or her stock options, the Peeper Entities would sell shares of Starnet common stock to the public equal to the number of shares to be issued upon exercise of the relevant stock options. Plan Shares then were transferred to the Peeper Entities to complete the "swap" transaction and were resold by the Peeper Entities to the public. 34/ In total, from January to October 1999, the Peeper Entities purchased 4.9 million shares of Starnet common stock through the exercise of the warrants and piggyback warrants in addition to the 2.45 million 1997 Shares. From January 1999 through February 2001, the Peeper Entities sold more than 5.2 million shares of Starnet common stock (comprising the 1997 Shares, the Plan Shares, and shares received upon exercise of the warrants and piggyback warrants) to the public. The more than 5.2 million shares sold by the Peeper Entities to the public represented a significant percentage of Starnet's outstanding stock during this period. 35/

33/ (...continued)
resales made in reliance on the safe harbor provided by Rule 904: first, such offer or sale must be made in an "offshore transaction" by any person other than an issuer, a distributor, an affiliate of either (other than specified officers and directors) and any person acting on behalf of any of the foregoing, and second, no "directed selling efforts" may by made in the United States in connection with an offer or sale of securities in reliance on the safe harbor. Here, the resales were made by Peeper Entities in their role as the conduit of Starnet common stock from Starnet to the public, and the resales were directed by Peeper, Geiger, Kaufmann, and Gould to the public within the United States.

34/ Geiger incorrectly asserts that the law judge improperly integrated Starnet's offering of the 1997 Shares with the sale of the Plan Shares. The law judge found, as described above, that the resale -- not the original offering -- of the 1997 Shares was part of the effort to distribute unregistered securities.

35/ As of October 31, 1998, prior to the commencement of the distribution, Starnet reported 22,450,000 shares of common stock outstanding. See Form 10-QSB for the quarter ended October 31, 1998. As of January 31, 2000, Starnet reported 31,531,488 shares outstanding. See Form 10-QSB for the quarter ended January 31, 2000.

We find that the Peeper Entities were underwriters. The Peeper Entities purchased Starnet common stock on the exercise of the warrants and piggyback warrants with a view to the distribution of such shares. They resold those shares, along with the 1997 Shares and the Plan Shares, in connection with a distribution in order to fund the option exercises of Starnet Option Holders. Accordingly, because the Peeper Entities acted as a conduit beginning in January 1999 for the distribution to the public of the 1997 Shares, the Plan Shares, and shares received upon exercising the warrants and piggyback warrants that had been commingled together, they functioned as statutory underwriters for such distribution, and any sales in connection therewith were not exempt from registration under Section 4(1) of the Securities Act. 36/

b. "Section 4(1 ½)"

Carley and Zacharias each contend that their sales of the Plan Shares were exempt from registration pursuant to the so-called Section 4(1 ½) exemption because the sales were made in private transactions to the Peeper Entities and not to the public. Geiger similarly contends that the sales of the Plan Shares were exempt as private transactions because the shares were sold to the Peeper Entities in private transactions and not to the public. The Section 4(1 ½) exemption is a "hybrid exemption" not specifically provided for in the Securities Act that basically allows "affiliates to make private sales of securities held by them so long as some of the established criteria for sales under both Section 4(1) and Section 4(2) of the Act are satisfied." 37/ As with the other exemptions from the registration requirements, persons claiming such an exemption have the burden of establishing that such sales do not constitute a public distribution. 38/ Respondents have not met this burden.

36/ We further reject the argument that the exemption provided by Section 4(1) applies to the resale of the 1997 Shares issued to the Peeper Entities pursuant to Regulation S. We have made clear that a person who acts as an underwriter may not resell Regulation S stock absent registration. Problematic Practices Under Regulation S, Securities Act Rel. No. 7190 (June 27, 1995), 59 SEC Docket 1998.

37/ Employee Benefit Plans, Securities Act Rel. No. 6188 (Feb. 1, 1980), 19 SEC Docket 465, 496 n.178; see also, e.g., United States v. Lindo, 18 F.3d 353, 358 (6th Cir. 1994); SEC v. Cavanagh, 1 F. Supp. 2d 337, 368 (S.D.N.Y. 1998); Louis Loss and Joel Seligman, Fundamentals of Securities Regulation 338 (3d ed. 1995); Hicks, Exempted Transactions Under The Securities Act of 1933 § 9.05 (1992); The Section "4(1) ½" Phenomenon: Private Resales of "Restricted" Securities, 34 Bus. Law. 1961 (1979). This implied exemption, which allows affiliates to sell substantial amounts of their shares to private investors, has been referred to as the 4(1½) exemption because it falls between the 4(1) and 4(2) exemptions, which allow, respectively, for sales among persons who are not issuers, underwriters, or dealers, and for private sales by an issuer. Cavanagh, 1 F. Supp. 2d at 368.

38/ See Cavanagh, 1 F. Supp. 2d at 368-69.

Carley, Zacharias, and the other Starnet Option Holders sold their Plan Shares to the Peeper Entities to replace the Starnet shares that the Peeper Entities had owned and previously sold to the public on behalf of Starnet Option Holders. The Plan Shares sold to the Peeper Entities were, in short order, resold to the public. Thus, the sales to the Peeper Entities were a necessary and critical step in the overall distribution of shares to the public. Carley and Zacharias knew, or should have known, of the Peeper Entities' role as the conduit of shares of Starnet common stock to the public. Accordingly, because these sales were not made in private transactions but were instead a necessary step in the distribution of securities to the public, they do not qualify for exemption under the registration requirements. 39/

c. Securities Act Section 4(4)

With respect to their own participation in the distribution of securities, Geiger and Kaufmann assert that the broker's exemption contained in Section 4(4) of the Securities Act, which exempts "brokers' transactions executed upon customers' orders on any exchange or in the over-the-counter market but not the solicitation of such orders" from the registration requirements of Securities Act Section 5, is available. However, this exemption – which is designed to exempt ordinary brokerage transactions – is not available to a registered representative if he knows or has reasonable grounds to believe that the selling customer's part of the transaction is not exempt from Section 5 of the Securities Act. In that event, the registered representative likewise violates Section 5 of the Securities Act by virtue of participating in a non-exempt transaction. 40/ The amount of inquiry required of the broker necessarily varies with the circumstances of each case; however, "when a dealer is offered a substantial block of a little-known security . . . where the surrounding circumstances raise a question as to whether or not the ostensible sellers may be merely intermediaries for controlling persons or statutory underwriters, then searching inquiry is called for." 41/

39/ Cf. Earl J. Knudson & Co., 40 S.E.C. 599, 604 (1961) ("Under all the circumstances, we find that an illegal public distribution of International stock by controlling interests was effected and that Knudson participated in significant steps essential thereto and aided and abetted in such distribution. It is apparent that in light of the extensive distribution, no private offering exemption under Section 4(1) as claimed by Knudson was available.").

40/ See United States v. Wolfson, 405 F.2d 779, 782-83 (2d Cir. 1968), cert. denied, 394 U.S. 946 (1969); Loss & Seligman, supra note 37, at 1463; Wonsover, 54 S.E.C. at 13 n.27 (citing Quinn & Co., 44 S.E.C. at 468); Robert G. Leigh, 50 S.E.C. 189, 193 (1990) (noting that "the duty of inquiry extends to salesmen").

41/ Distribution By Broker-Dealers of Unregistered Securities, Securities Act Rel. No. 4445 (Feb. 2, 1962) (footnote omitted) (quoting SEC v. Culpepper, 270 F.2d 241, 251 (2d Cir. 1959)); see also Kane v. SEC, 842 F.2d 194, 199 (8th Cir. 1988); Wonsover, 54 S.E.C. at 14; Leigh, 50 S.E.C. at 193 (stating that "the duty of inquiry extends to salesmen").

Kaufmann and Geiger were responsible for executing a large number of transactions in a little-known security over a short period of time. Through this procedure, the Peeper Entities sold more than 5.2 million shares of Starnet common stock to the public. Kaufmann and Geiger knew or should have known that the Peeper Entities' sales of shares of Starnet common stock were part of an unlawful distribution. Kaufmann and Geiger helped to structure the steps in the distribution and had knowledge that the Peeper Entities agreed to sell shares of Starnet common stock to the public in order to fund the option exercises of Starnet's Option Holders, including Starnet directors and executive officers. Geiger knew that Starnet stock was being placed into the Peeper Entities' and Starnet officers' accounts at Spencer Edwards and sold to the public shortly thereafter. Kaufmann testified that he knew the Peeper Entities' accounts were selling Starnet stock on a "fairly continuous" basis. The trading instructions that Kaufmann received from Gould with respect to the Peeper Entities' accounts usually did not refer to a specific account, indicating that the accounts were being used as a fungible pool of stock that was sold to the public in order to facilitate the exercise of stock options by Starnet's officers and employees. Along with Gould, Kaufmann kept a running total of the stock being sold by the Peeper Entities' accounts. Kaufmann and Geiger also processed orders to wire the proceeds from the sale of Starnet stock by the Peeper Entities to the Brovarone trust accounts. Despite these facts, which strongly indicated that an unregistered distribution of Starnet stock was being accomplished through the Peeper Entities, Kaufmann and Geiger failed to make the searching inquiry required of them under these circumstances. Accordingly, Kaufmann and Geiger either knew or should have known that their clients' sales of Starnet common stock violated the provisions of Section 5 of the Securities Act; hence, Section 4(4) is not available to exempt their transactions. 42/

d. "Free Trading" Stock

Kaufmann argues that a July 1996 offering of 10 million shares by Starnet's predecessor pursuant to Rule 504 of Regulation D created a freely-trading public float. 43/ In his brief, Kaufmann maintains that these 10 million shares were commingled with the 1997 Shares and the

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42/ For the same reason, Geiger's argument that the Starnet officers' sales complied with Rule 144 fails. Rule 144 requires that sales pursuant to Rule 144 comply with Securities Act Section 4(4). Rule 144(g), 17 C.F.R. § 230.144(g). As discussed above, these sales did not. Nor had the officers satisfied the holding period for the sale of the Plan Shares. A new holding period begins upon exercise of the option. See Resales of Restricted and Other Securities, Securities Act Rel. No. 6099 (Aug. 2, 1979), 17 SEC Docket 1422, 1432 (stating that Rule 144 "permits tacking only if the consideration surrendered upon exercise of the warrants consists solely of other securities of the same issuer" and that where the consideration includes cash "the exercise of the warrants is deemed to involve the acquisition of new restricted securities for which tacking is not permitted").

43/ Rule 504 of Regulation D, 17 C.F.R. § 230.504, as in effect in 1996, permitted a non-reporting issuer to offer and sell securities without filing a registration statement, so long as the offer and sale was limited to $1 million in any twelve-month period.

Plan Shares in the Spencer Edwards accounts of the Peeper Entities and Starnet's officers and, therefore, there is no evidence in the record that any single share sold from these accounts "was other than a free trading share."

The record is clear that the Peeper Entities purchased their shares of Starnet common stock directly from Starnet, either in the Regulation S offering, which closed in December 1997, or through the exercise of warrants and piggyback warrants in 1999, and that it was these shares, along with shares of Starnet stock issued upon exercise of stock options and transferred to the Peeper Entities and commingled with the other shares, that were resold to the public as part of the distribution. Moreover, assuming that the July 1996 offering complied with the provisions of Rule 504, any resale of the shares had to be registered or qualify for an exemption. 44/ The Division established that there was never a registered public offering of Starnet stock, and Kaufmann has failed to establish that, with one possible exception cited by the law judge involving 100,000 shares, any subsequent transactions in the 10 million shares were exempt from registration. 45/

2. Participant Liability for Section 5 Violations

To show that a person bears participant liability for a Section 5 violation, the Division must prove that the person was a "necessary participant" or "substantial factor" in the violation. 46/ Even where the person or entity does not have individual contact with the purchasers of the securities, that person or entity has indirectly offered or sold the security to the

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44/ See Preliminary Note 4 to Regulation D, 17 C.F.R. §§ 230.501-.508 ("These rules are available only to the issuer of the securities and not to any affiliate of that issuer or to any other person for resales of the issuer's securities. The rules provide an exemption only for the transactions in which the securities are offered or sold by the issuer, not for the securities themselves.").

45/ Kaufmann and Price also objected to four of the Division's exhibits summarizing the sale of Starnet stock on the basis that the transactions reflected therein could include the alleged 10 million shares that were free trading public float. Respondents have failed to establish that the resales of this stock previously issued under Rule 504 were either registered or entitled to an exemption and, therefore, there is no basis for excluding the challenged Division exhibits.

46/ SEC v. Calvo, 378 F.3d 1211, 1215 (11th Cir. 2004); see also Holschuh, 694 F.2d at 139-40; Murphy, 626 F.2d at 649-52.

public "if he or it has employed or directed others to sell or offer them, or has conceived of and planned the scheme by which the unregistered securities were offered or sold." 47/

Carley and Zacharias each contend that the record does not support a finding that they participated in sales of securities in violation of the registration requirements of Section 5. 48/ The record establishes that Carley and Zacharias each participated in the unregistered distribution of securities and received proceeds from the Peeper Entities in connection with their exercise of stock options. Both Carley and Zacharias executed Gould's irrevocable authorization acknowledging that "certain shares will be sold" on their behalf prior to the receipt of the Plan Shares and that Gould would transfer the shares received in their name "into an appropriate account in order to reimburse for the shares sold on my behalf." What Carley characterizes as "control accounts" at Spencer Edwards were opened for both Carley and Zacharias through which Starnet stock was sold, and each received monthly statements for these accounts. Thus, Carley and Zacharias were necessary participants in the unregistered transactions through which they exercised and sold their stock options. 49/

47/ SEC v. Friendly Power, 49 F. Supp. 2d 1363, 1371 (S.D. Fla. 1999); see also Holschuh, 694 F.2d at 140 ("To hold that proof of direct contact [with investors] is necessary would be to ignore and render meaningless the language of Section 5, which prohibits any person from 'directly or indirectly' engaging in the offer or sale of unregistered securities.").

48/ Zacharias contends that the law judge found that Zacharias violated Section 5 only in connection with sales of his own stock and rejected the contention that he violated Section 5 in any other way. The law judge, however, concluded that Zacharias was directly involved in the sale of his own shares and indirectly involved in the sale of Plan Shares by Starnet's Option Holders.

49/ Carley argues that he did not become an officer of Starnet until October 1997 and that he worked for Starnet on a part-time basis until March or April 1998, at which time he assumed full-time status. He contends that these facts establish that he was not a participant in the unregistered sale of Starnet stock and that the law judge violated his due process rights by finding that Carley had been a Starnet director since January 1997.

It is unclear how Carley's claim that he did not become a full-time officer until April 1998 supports his contention that he did not violate the registration requirements. Carley does not dispute that he was a full-time Starnet officer in January 1999, when Starnet began its unregistered distribution through the Peeper Entities' purchase and sale of Starnet stock obtained upon the exercise of the warrants and piggyback warrants and when he began to exercise his stock options. Thus, he was a substantial participant in the sale of unregistered Starnet stock regardless of when he became an officer of the company.

(continued...)

Moreover, Zacharias was involved in structuring the various steps of the distribution. He first discussed with Gould the inability of Starnet Option Holders to resell their Plan Shares in Canada. He was responsible for directing the transfer agent to issue Starnet stock upon the Peeper Entities' exercise of the warrants and piggyback warrants, making that stock available to be sold as part of an unregistered distribution. As an addressee on Brovarone's memorandum, he clearly knew the process by which the plan to distribute Starnet stock was being effectuated. 50/

Kaufmann and Geiger were also necessary participants and substantial factors in the sale of unregistered Starnet stock. Kaufmann and Geiger were account executives on the Spencer Edwards accounts of the Peeper Entities, of Carley, Zacharias, other Starnet officers, and of Celestine. Under their joint account number, they executed the trades in Starnet stock for these accounts. 51/

Geiger claims that he cannot be liable as a participant because he acted as "one who simply brokers a transaction . . . and receives usual and customary compensation." Geiger understates his involvement. In 1997, Geiger took two trips to Vancouver to meet with Starnet officers, and he recommended that Peeper participate in the 1997 Regulation S offering. 52/ Later, he met with Gould regarding the plan to "swap" the Peeper Entities' shares for the Plan Shares, and he informed Peeper that stock held by Starnet's employees and officers might become available. Geiger knew that the Peeper Entities were purchasing large quantities of Starnet stock from the exercise of the warrants and piggyback warrants (as well as receiving Plan Shares) and shortly thereafter selling them to the public. 53/ Indeed, Geiger executed most of these trades.

49/ (...continued)
In any event, Carley admitted in his answer to the OIP that he was Starnet's chief financial officer from at least March 10, 1997, although he now claims that this admission was incorrect. Amendment No. 1 to Form 10-SB, filed August 14, 1997, and Form 10-KSB, filed July 30, 1999, also state that Carley became a Starnet director on January 27, 1997.

50/ See supra note 13.

51/ Although Geiger executed most of the sales from the Peeper Entities' accounts, Kaufmann testified that he executed at least some of the sales from the Peeper Entities' accounts.

52/ Geiger also received valuable consideration from the Peeper Entities. See supra note 19.

53/ Geiger v. SEC, 363 F.3d 481, 487 (D.C. Cir. 2004) (holding that a person responsible for "finding the buyer, negotiating the terms, [and] facilitating the resale" is a participant in the sale of unregistered securities).

Kaufmann asserts that he was a fringe participant in these transactions. Kaufmann communicated frequently with Gould. He accepted orders from Gould and ensured that Brovarone had funds to wire as directed by Gould. Kaufmann tracked the transactions in Starnet stock from the Peeper Entities' accounts and knew that it did not matter which Peeper Entities' accounts sold stock to facilitate the exercise of the Starnet Plan options and that the shares of Starnet stock held in the Peeper Entities' accounts were treated as being fungible. He completed Forms 144 in connection with the sales of Plan Shares from Starnet officers' Spencer Edwards accounts.

Kaufmann argues that he took steps to assure that Starnet securities could lawfully be sold. For example, Kaufmann created a form for Spencer Edwards's use in investigating the history of stock certificates. During an examination of Spencer Edwards by Commission staff in August 1999, Kaufmann asked a Commission examiner whether Kaufmann had correctly completed two sets of Forms 144 for Starnet officers and directors with respect to their sale of Starnet stock. Kaufmann stated that, while the examiner "didn't do detailed research into it," he thought that the two Forms 144 "appeared, at least in form, to be filled out properly." When he encountered a stock certificate in the name of a predecessor company of Starnet with which he was unfamiliar, he discussed his concerns with Brovarone and the transfer agent. Nevertheless, Kaufmann's actions fell short of the searching inquiry required given the numerous indications that the millions of shares of Starnet stock that were being sold through accounts at Spencer Edwards were part of an unregistered distribution. Indeed, when he asked Brovarone about the predecessor corporation stock certificate, Brovarone warned him that all affiliates' stock was restricted and unregistered stock could not be sold. As demonstrated above, Kaufmann disregarded this advice.

Accordingly, we conclude that Carley, Zacharias, Kaufmann, and Geiger are each liable as participants in the offer or sale of unregistered securities.

3. Advice of Counsel

Geiger and Kaufmann each argue that they properly relied on the advice of counsel. Reliance on the advice of counsel requires that a respondent "made complete disclosure to counsel, sought advice as to the legality of his conduct, received advice that his conduct was legal, and relied on that advice in good faith." 54/ Geiger and Kaufmann produced no evidence that they disclosed the mechanics of the swap transactions to an attorney and received advice that those transactions complied with the securities laws.

Although the record contains several opinion letters discussing isolated components of the swap transactions, no letter addresses the legality of the plan to swap Starnet common stock held by the Peeper entities for Plan Shares issued to Starnet's Option Holders. Kaufmann

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54/ Markowski v. SEC, 34 F.3d 99, 104-05 (2d Cir. 1994) (citing SEC v. Savoy Indus., Inc., 665 F.2d 1310, 1314 n.28 (D.C. Cir. 1981)).

contends that counsel "issued opinions regarding the propriety and legality of removing the restrictive legends from the shares utilized in the employee stock option process," 55/ but these letters do not analyze the propriety or legality of swapping the shares acquired by the Peeper entities pursuant to the Regulation S offering for the shares issued to Starnet's Option Holders under the stock option plans. 56/ In 1997, Brovarone wrote Starnet's transfer agent opining that the sale of the 1997 Shares was "exempt" from registration pursuant to Regulation S and that the stock certificates could be issued without restrictive legends. In December 1998, attorney Scott Reed gave Zacharias an opinion that Starnet could also issue the shares obtained by the Peeper Entities upon exercise of the warrants without restrictive legends. Geiger and Kaufmann could not rely on either opinion because both discussed only the legality of issuing the shares without a restrictive legend and did not address the legality of swapping those shares for Plan Shares.

Brovarone's opinion letters discussing Rule 144 transactions by Starnet officers also involved only one component of the swap transactions. These opinion letters expressed only the opinion that Starnet was current in its filings, that Starnet and its management did not know of any reason why the proposed sale could not be made within ninety days under Rule 144, that the number of shares sold or planned to be sold by the shareholder was less than the greater of one percent of the outstanding shares of common stock or the average weekly volume for the past four weeks, and that the shareholder was exempt from registration pursuant to the Securities Act of British Columbia. Brovarone also rendered his opinion after his "review of the attached documentation, and in reliance upon certain representations made by the Shareholder," which included the representation that the seller was "not individually, or together with others, engaged in making a distribution of a substantial amount of such securities, and has no intention of making or participating in such distribution." Geiger and Kaufmann knew that the transaction described in the opinion letter was only one step in the process of swapping Starnet common stock held by the Peeper entities for Plan Shares issued to Starnet's Option Holders. The Rule 144 opinion letters did not opine on the legality of this process.

55/ A restrictive legend is "a statement place on restricted stock notifying the holder that the stock may not be resold without registration." Charles F. Kirby, Securities Act Rel. No. 8174 (Jan. 9, 2003), 79 SEC Docket 1081, 1084, petition denied sub nom. Geiger v. SEC, 363 F.3d 481 (D.C. Cir. 2004). The absence of a restrictive legend on stock certificates, however, does not "warrant the conclusion that they must be freely tradable." Gilbert F. Tuffli, Jr., 46 S.E.C. 401, 409 (1976).

56/ Geiger and Kaufmann also may not rely on Canadian counsel's opinion letter that proposed transferring the Plan Shares out of British Columbia and then reselling them because Starnet never implemented this hypothetical structure. See supra note 9. Geiger suggests that Gould fulfilled a role akin to the non-Canadian trustee suggested by counsel. There is no suggestion in the record, however, that Gould, a Vancouver resident, acted other than as an associated person of United Capital, a broker-dealer.

The only document which discusses the entirety of the swap transaction process is Brovarone's September 1999 memorandum. We reject Kaufmann's assertion that this document "was, in and of itself, a legal opinion validating the stock option process which is the subject of this administrative proceeding." This memorandum simply recited the steps involved in the swap transactions and did not opine on their legality. We therefore reject the argument that Geiger and Kaufmann properly relied on the advice of counsel because they produced no evidence that an attorney provided advice that the swap transactions complied with the securities laws. 57/

Geiger and Kaufmann also claim reliance on the removal of restrictive legends from Starnet officers' stock certificates by Starnet's transfer agent. We have held that "a securities professional cannot rely on the determination of a transfer agent that stock is free trading." 58/

57/ Cf. SEC v. McNamee, 481 F.3d 451, 456 (7th Cir. 2007) (rejecting advice of counsel defense because defendant "did not produce any letter from a securities lawyer giving advice that reflected knowledge of all material facts"); see also Wonsover, 205 F.3d at 415 (finding that "[p]recedent will not suffer [respondent's] argument that he justifiably relied on the clearance of sales by [the restricted stock department], the transfer agent and counsel" because an "investment executive . . . has the primary responsibility to prevent illegal sales of restricted or control stock").

58/ Kirby, 79 SEC Docket at 1092 n.34 (citing Wonsover, 54 S.E.C. at 15 (finding that registered representative was not relieved of his obligation to explore whether shares are freely tradeable "simply because the transfer agent and Restricted Stock Department eventually cleared the stock"); Leigh, 50 S.E.C. at 194 (finding that, "as the courts and this Commission have held, the transfer agent's willingness to reissue the certificates without restrictive legends did not relieve [the registered representative] of his obligation to investigate")).

Kaufmann and Geiger each claim that their violations of Securities Act Section 5 were not "willful" within the meaning of Exchange Act Section 15(b)(4), 15 U.S.C. § 78o(b)(4). Exchange Act 15(b) authorizes the Commission to impose certain sanctions based on willful violations of the securities laws. A "willful violation of the securities law . . . means merely the intentional commission of an act which constitutes the violation and does not require that the actor 'also be aware that he is violating one of the Rules or Acts.'" Wonsover, 205 F.3d at 414 (quoting Gearhart & Otis, Inc. v. SEC, 348 F.2d 798, 803 (D.C. Cir. 1965)); see also V.F. Minton, 51 S.E.C. 346, 352 (1993), aff'd, 18 F.3d 937 (5th Cir. 1994) (Table). At best, Kaufmann and Geiger closed their eyes to suspicious facts suggesting that the Starnet stock being sold through Spencer Edwards constituted an unregistered distribution, and they ignored the obvious need for further inquiry in violation of their duties as registered representatives of a broker-dealer. In so doing, they willfully violated Securities Act Sections 5(a) and 5(c).

* * *

We conclude that the offers and sales of Starnet stock at issue here were not registered under the Securities Act, that Carley, Zacharias, Geiger, and Kaufmann participated in the sale of unregistered Starnet stock, and that the sales at issue here did not fall within any applicable exemption to the registration requirements. As a result, in accordance with Securities Act Section 8A and Exchange Act Section 21C, we find that Carley and Zacharias violated Securities Act Sections 5(a) and 5(c), and, in accordance with Exchange Act Section 15(b), we find that Geiger and Kaufmann willfully violated Securities Act Sections 5(a) and 5(c). 59/

V.

Supervision of Geiger and Kaufmann

A. Edward Price has been president, CEO, branch manager, and compliance officer for Spencer Edwards since March 1994. Price was responsible for supervising Kaufmann and Geiger during the events at issue in this proceeding, as well as for overseeing the daily operations of Spencer Edwards. As part of his responsibilities, Price organized and ran annual compliance meetings and ultimately was responsible for compliance matters at Spencer Edwards. Price testified that his compliance responsibilities comprised "anything of a legal nature that was part of our procedures."

Geiger and Price were respondents in a previous Commission administrative proceeding involving stock sales as part of an unregistered distribution in violation of Securities Act Section 5 by one of the Peeper Entities involved in this proceeding (the "Kirby proceeding"). 60/ Price

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59/ The law judge also found that sales of Starnet stock by Madison Park Trust, a trust for which Carley and his wife were the sole beneficiaries, violated Securities Act Sections 5(a) and 5(c). We have determined, given the lack of evidence in the record before us in this proceeding, to dismiss the allegation that these sales were part of an unregistered distribution in violation of Securities Act Sections 5(a) and 5(c).

60/ Geiger was charged with willfully violating Securities Act Section 5. Price was charged with failing to supervise Geiger. We found that Geiger willfully violated Section 5 in the offer and sale of two blocks of Golden Eagle International, Inc. stock, totaling roughly 2.8 million shares, by LaSalle Investments, Ltd., one of the Peeper Entities involved in this proceeding. We barred Geiger from association with any broker or dealer with a right to reapply after five years and from participation in any penny stock offering, ordered him to cease and desist from violations or future violations of Securities Act Section 5, and ordered him to pay $14,109.21 in disgorgement and a civil penalty of $300,000. Charles F. Kirby, Securities Act Rel. No. 8174 (Jan. 9, 2003), 79 SEC Docket 1081, petition denied sub nom. Geiger v. SEC, 363 F.3d 481 (D.C. Cir. 2004). The law judge found

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responded to the investigation in the Kirby proceeding by placing Geiger and Kaufmann on "special supervision." Price placed Geiger on special supervision after Spencer Edwards determined that, in connection with the Kirby proceeding, Geiger failed to engage in a searching inquiry into the origin of securities to ensure that he was not facilitating an unregistered sale. Price removed Geiger from special supervision after Spencer Edwards determined that Geiger was "now capable of identifying the circumstances which give rise to a higher than usual level of scrutiny before engaging in a particular transaction." Geiger's special supervision lasted from September 1996 to September 1997. Kaufmann was not a respondent in the Kirby proceeding, but Price learned during the investigation in that proceeding that Kaufmann had signed a broker-dealer representation letter required under Rule 144 without authority to do so. Price placed Kaufmann on special supervision from September 1996 to March 1997. 61/

Price maintained that, although he did not return Geiger and Kaufmann to "special" supervision following the hearing in the Kirby proceeding, he exercised what he characterized as "heightened supervision" over all the transactions conducted by Geiger and Kaufmann. 62/ However, Price allowed Geiger and Kaufmann to share a separate private office. That office included a separate facsimile machine. Price testified that he "assumed if there was anything of

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60/ (...continued)
that Price had not failed reasonably to supervise Geiger and dismissed the proceeding against him. We declared that determination final. Kirby, 79 SEC Docket at 1082 n.3.

61/ Price also called a special compliance meeting in September 1996 after giving investigative testimony in the Kirby proceeding. All registered representatives, including Kaufmann and Geiger, were required to attend. Until that time, Spencer Edwards's salespersons had verified the origin of a stock certificate by checking with the transfer agent and speaking with the issuer and the customer. Price told the registered representatives that a more searching inquiry was required before processing transactions. Spencer Edwards also sent a memorandum to all its brokers listing several red flags, such as certificates delivered into foreign accounts and certificates for large blocks of stock relative to the stock's average trading volume, that indicated the need for a more searching inquiry into a stock certificate.

62/ Price stated in his investigative testimony in the instant proceeding that the trial in the Kirby proceeding was an "eye-opening" experience regarding Geiger. According to Price, Geiger "lied about the whole thing." Price testified further at the hearing in this proceeding that "[m]any of the things that we had thought in the compliance department to be true . . . turned out to be incorrect."

importance they would bring me the fax like everybody in the firm did." 63/ Price acknowledged that he never saw any of the numerous facsimiles exchanged between Kaufmann and Gould. 64/

Price testified that he reviewed the account activity in the Peeper Entities' accounts as part of his heightened supervision. Price knew that both Geiger and Kaufmann were the account executives for the Peeper Entities' accounts and that the Peeper Entities' accounts were "very active." He saw that the Peeper accounts were selling large amounts of Starnet stock into the market starting in January 1999. Price asked Geiger and Kaufmann about these transactions. He testified that they told him "that the employees of Starnet were exercising their stock options and that Mr. Peeper was buying them in a private transaction and selling them back into the market, and that they were registered under S-8." Price learned, as the Starnet shares continued to come through the accounts, that some of the stock being sold by the Peeper Entities' accounts was acquired through the exercise by the Peeper Entities of warrants and piggyback warrants issued as part of an earlier Regulation S offering.

Price testified that he did not request to see any opinion letters associated with the Starnet stock being sold in the Peeper accounts even though his understanding was that Regulation S shares could not be "sold back into the United States except in certain circumstances." He simply asked Geiger and Kaufmann if opinion letters "existed" and if Geiger and Kaufmann "felt comfortable with the transactions." Price also testified that he "questioned" Geiger and Kaufmann about the transactions involving Starnet. He asked Geiger and Kaufmann whether they had met all of the firm's requirements with respect to these transactions and whether they had gone further than they usually would on a regular transaction. Price testified that Geiger and Kaufmann answered these questions affirmatively. Price admitted that he did not himself do anything to investigate the source of the stock.

Price also testified that he reviewed the Starnet officers' Rule 144 transactions. He stated that he knew Carley and Zacharias opened accounts at Spencer Edwards, that he associated these accounts with the sale of control stock, and that Kaufmann prepared most of the Rule 144 paperwork with respect to the sale of control stock through the Starnet officers' accounts. Price admitted that the Forms 144 associated with these sales were never filed with the Commission. Price further acknowledged certain inaccuracies, such as the number of outstanding shares of Starnet, on the Forms 144. Price testified that he was not responsible for the accuracy of the information on the forms and that the obligation to ensure that the forms contained correct information rested with the account executive.

63/ Spencer Edwards's compliance manual provided, among other requirements, that all incoming correspondence "be reviewed by the Operations Manager or the Compliance Department prior to distribution" and that all "correspondence or other written communication with a customer or prospective customer which relates to [Spencer Edwards] and its business shall be reviewed prior to mailing or delivery."

64/ Price also did not see the few facsimile messages addressed to Geiger.

B. Exchange Act Sections 15(b)(6) and 15(b)(4)(E) provide that we may sanction a person associated with a broker-dealer if we find that such person failed reasonably to supervise, with a view to preventing violations of the federal securities laws and rules and regulations thereunder, another person who commits such violations if such person is subject to the individual's supervision. 65/ No person shall be deemed to have failed reasonably to supervise any other person if (i) there have been established procedures, and a system for applying such procedures, which would reasonably be expected to prevent and detect, insofar as practicable, any such violation by such other person, and (ii) such person has reasonably discharged the duties and obligations incumbent upon him by reason of such procedures and system without reasonable cause to believe that such procedures and system were not being complied with. 66/

We find that Price failed reasonably to supervise Kaufmann and Geiger. Supervision of an associated person must be "reasonable . . . under the attendant circumstances." 67/ Here, Price knew that Geiger had previously been charged with offering and selling unregistered securities from an account in the name of one of the Peeper Entities involved in this proceeding. He also believed that Geiger had lied to him about transactions involving unregistered stock in the Kirby proceeding. Price knew further, as a result of the investigation in the Kirby matter, that Kaufmann had signed a Rule 144 broker-dealer representation letter without authority to do so. These facts highlighted the need for Price's heightened supervision over Geiger and Kaufmann, especially regarding unregistered sales of securities and alleged Rule 144 transactions. 68/ Under these circumstances, Price had a particular responsibility to ensure not only that rules and procedures were in place to supervise Geiger and Kaufmann properly, but also that those rules and procedures were enforced. 69/

65/ 15 U.S.C. §§ 78*o*(b)(6), (b)(4)(E).

66/ Id.

67/ Clarence Z. Wurtz, 54 S.E.C. 1121, 1130 (2001) (quoting Arthur James Huff, 50 S.E.C. 524, 528-29 (1991)); see also Louis R. Trujillo, 49 S.E.C. 1106, 1110 (1989) (stating that supervision must be reasonable "under all the circumstances").

68/ See John A. Chepak, 54 S.E.C. 502, 514 (2000) (stating that "prior misconduct indicated the need for heightened supervision, particularly in areas that had resulted in previous violations"); see also Consol. Invs. Servs., Inc., 52 S.E.C. 582, 588-89 (1996) (stating that an employee who has previously evidenced misconduct can only be retained if he subsequently is subjected to a commensurately higher level of supervision).

69/ See Wurtz, 54 S.E.C. at 1130 (stating that supervisors who know of an employee's past disciplinary history must ensure not only that rules and procedures are in place to supervise the employee properly, but also that those rules and procedures are enforced).

The procedures Price instituted in response to the misconduct in the Kirby proceeding were inadequate. "We have repeatedly stressed that supervisors cannot rely on the unverified representations of their subordinates." 70/ Here, however, Price relied primarily on Geiger's and Kaufmann's statements in reviewing their account activity. 71/ Price conducted his review of the Starnet sales by asking Geiger and Kaufmann whether they were "comfortable with the transactions," whether they had "met all of [the firm's] requirements with these transactions," and whether they had "gone further than [they] usually would on a regular transaction." Price testified further that he did not request to see any opinion letters associated with the Starnet stock being sold out of the Peeper accounts and simply asked Geiger and Kaufmann "if they existed" and if Geiger and Kaufmann "felt comfortable with the transactions." We find this method for assessing the activity in the Peeper accounts "woefully inadequate." 72/

We have held previously that "any indication of irregularity brought to a supervisor's attention must be treated with the utmost vigilance." 73/ Price knew that the Peeper accounts were selling large amounts of Starnet stock. Geiger and Kaufmann told him that Peeper was buying Plan Shares and selling them back into the market. Price learned that Peeper bought the Plan Shares by selling Starnet shares previously obtained through the exercise of warrants and piggyback warrants tied to an earlier Regulation S offering. He testified that he knew Regulation S shares "could not be sold back into the United States except under certain circumstances." Price knew further that the misconduct in the Kirby case involved unregistered sales allegedly pursuant to Regulation S of securities in accounts controlled by Peeper. He acknowledged that he considered the Kirby proceeding an "eye-opening" experience. However, although Price maintained that he exercised "heightened supervision" over Geiger and Kaufmann following the Kirby proceeding, Price allowed Geiger and Kaufmann to retain a private office with a separate facsimile machine. Price also "questioned" Geiger and Kaufman with respect to the sales of Starnet stock in the Peeper Entities' accounts, but when asked whether he himself did "anything to investigate the source of the stock," he answered no. Price's failure to monitor more closely Geiger and Kaufmann's transactions and conduct his own investigation into these transactions was unreasonable, particularly in light of the previous Regulation S-related misconduct and the

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70/ Quest Capital Strategies, 55 S.E.C. 362, 372 (2001) (citing John H. Gutfreund, 51 S.E.C. 93, 108 (1992) and Michael H. Hume, 52 S.E.C. 243, 248 (1995)).

71/ As noted, Price had previously instructed Spencer Edwards's registered representatives to conduct a searching inquiry regarding unregistered stock and to do more than rely on the word of the transfer agent, issuer, or customer.

72/ Cf. Quest Capital Strategies, 55 S.E.C. at 374 (finding that, although respondents had a comprehensive set of rules, respondents' system for applying the rules to the misconduct at issue was "woefully inadequate" because "[r]elying on a subordinate's assurances is hardly an effective method of preventing or detecting violations").

73/ See Consol. Invs. Servs., 52 S.E.C. at 588.

evidence of numerous ongoing Regulation S-related sales and sales of the Plan Shares as part of the distribution. 74/

Price's review of the Rule 144 paperwork prepared by Kaufmann was deficient, particularly in light of Kaufmann's past failure to follow firm procedures regarding such transactions. Price testified that he reviewed the Forms 144 prepared by Kaufmann, but he acknowledged the misstatement of the number of outstanding Starnet shares in certain of these forms. 75/ Price admitted further that the Forms 144 associated with these sales were never filed with the Commission. Price's supervisory review of the Rule 144 paperwork was cursory at best and constituted a failure of supervision. 76/

We reject Price's contention that the law judge improperly failed to consider the dismissal in the Kirby proceeding of the allegations that Price failed to supervise reasonably. The adequacy of supervisory procedures and their implementation necessarily depends on the facts and circumstances of each case. 77/ The circumstances which led the law judge in Kirby to conclude that Price's supervision was "reasonable" in that case are not present here. For example, in Kirby, the law judge concluded that Price "had no reason to think that Mr. Kirby would hide his activities from his review" and that Price "had no reason to think Mr. Geiger would lie about his dealings with the issuer and the issuer's attorney." 78/ At the time he was supervising the transactions at issue in this proceeding, however, Price knew, as he testified, that, with respect to the Kirby matter, Geiger had "lied about the whole thing."

74/ Cf. James J. Pasztor, 54 S.E.C. 398, 412-13 (1999) (finding failure to supervise where, in light of "many red flags" that employee was effecting wash trades and matched orders, supervisor "[a]t a minimum" "should have conducted an independent investigation"); Michael E. Tennenbaum, 47 S.E.C. 703, 711 (1982) (finding failure to supervise where, despite specific warnings that employee might be engaging in excessive trading, supervisor "failed to take or recommend any action to investigate [his] activities").

75/ Price testified that this error was not something he would have noticed at the time.

76/ See Blinder, Robinson & Co., 47 S.E.C. 812, 814 (1982) (finding respondents' "cursory examination" "clearly inadequate" because a failure of supervision "connotes 'a failure to learn of improprieties when diligent application of supervisory procedures would have uncovered them.'") (quoting Jerome F. Tegeler, 45 S.E.C. 512, 515 n.8 (1974) and Anthony J. Amato, 45 S.E.C. 282, 286 (1973)).

77/ La Jolla Capital Corp., 54 S.E.C. 275, 281 (1999).

78/ Charles F. Kirby, Initial Decision Rel. No. 177 (Dec. 7, 2000), 73 SEC Docket 3550, 3577, 3580.

We also reject Price's contention that finding violations of the registration provisions of the federal securities laws by the other Respondents "is inconsistent" with finding that Price failed to supervise because the covert nature of the violations "circumvented his ability to uncover and stop" the misconduct. The duty of supervision includes the responsibility to investigate red flags that suggest that misconduct may be occurring and to act upon the results of such investigation. 79/ Price's knowledge of the misconduct in the Kirby proceeding, which involved the unregistered sale of securities allegedly pursuant to Regulation S from accounts controlled by Peeper, as well as the numerous sales of Starnet stock in 1999 many of which were acquired in a Regulation S offering, demanded further investigation, which could have allowed Price to detect the violations of the securities laws. 80/ In addition to the red flags, Price might have discovered the misconduct had he monitored the facsimiles between Kaufmann and Gould. However, although Spencer Edwards required that a compliance officer review all client correspondence, Price allowed Geiger and Kaufmann to retain a separate facsimile machine in their private office even after the misconduct in the Kirby proceeding because he still "assumed if there was anything of importance they would bring me the fax like everybody in the firm did."

Price contends further that he did not fail to supervise reasonably because he relied on "green flags" provided by attorneys. He invokes the court's finding in Howard v. SEC 81/ that a broker did not recklessly aid and abet securities law violations because "rather than red flags, [he] encountered green ones, as outside and inside counsel approved [the transactions.]" According to Price, "Zoe Cole, a full-time compliance attorney who was Price's direct assistant, reviewed and supervised the transactions." Although Price testified that Cole reviewed unspecified opinion letters associated with Starnet's Regulation S offering and reviewed purported Rule 144 transactions by Starnet officers, no evidence suggests that she approved the resale of shares obtained pursuant to the Regulation S offering or the swap of those shares for Plan Shares. Price acknowledged that he did not discuss with Cole the issue of resales in the United States of stock issued pursuant to the Regulation S offering and that his understanding was that "Reg S shares could not be sold back into the United States except under certain circumstances." 82/

79/ Michael T. Studer, Exchange Act Rel. No. 50543A (Nov. 30, 2004), 84 SEC Docket 911, 922

80/ See Christopher J. Benz, 52 S.E.C. 1280, 1282 (1997) (rejecting contention that supervisor "could not have discovered" employee's violations because there were "numerous red flags" that supervisor "should not have ignored" such as employee's history of compliance problems and suspicious activities in employee's accounts).

81/ 376 F.3d 1136, 1147 (D.C. Cir. 2004).

82/ We also reject Price's contention that "[u]nder the ruling of Arthur James Huff, [50 S.E.C. 524 (1991)], Price cannot be disciplined in this matter. If there was deficient

(continued...)

Unlike in Howard, moreover, where the court found no "unusual circumstances" suggesting that the respondent acted recklessly, 83/ numerous red flags, as described above, existed here that suggested Geiger and Kaufmann were violating the securities laws. "When a broker ignores the obvious need for further inquiry, even in reliance on assurances from other brokers or attorneys, he violates the act." 84/ A broker has the primary responsibility to prevent illegal sales of restricted or control stock. 85/ Brokers are expected to have sufficient knowledge of the securities laws to investigate affirmatively when it appears that an offering may require registration. 86/ A supervisor may no more ignore the obvious need for further inquiry, even in reliance on assurances from an attorney, than may a salesperson.

Price also contends that he relied on attorney opinion letters authored by Reed and Brovarone regarding the legality of removing restrictive legends from the Starnet shares and selling Starnet shares pursuant to Rule 144. Price could not rely on the letters opining on the removal of restrictive legends because they did not deal with resales of the shares by the Peeper entities. 87/ The letters opining on the validity of individual Rule 144 transactions by Starnet officers did not relieve Price from conducting further searching inquiry. Even if the Rule 144 opinion letters authorized individual transactions by Starnet officers, Price knew of numerous additional sales of Starnet stock that should have put him on inquiry notice that the Rule 144

82/ (...continued)
supervision in this matter, Cole, not Price was the deficient supervisor and, therefore, Price cannot be disciplined." According to Price, the Commission held in Huff that "an individual cannot be disciplined for failing to supervise another individual who was in turn, a deficient supervisor." Price contends that "Cole was in fact, a supervisor who was in turn, supervised by Price." Price, however, was not charged with failing to supervise Cole, but with failing to supervise Geiger and Kaufmann. The record establishes that Price supervised Geiger and Kaufmann, and thus may be sanctioned for failing to supervise reasonably with a view to prevent their violations of the securities laws.

83/ 376 F.3d at 1149.

84/ Sorrell v. SEC, 679 F.2d 1323, 1327 (9th Cir. 1982).

85/ See Wonsover, 205 F.3d at 415 (rejecting broker's argument that he justifiably relied on the clearance of sales by the restricted stock department, the transfer agent, and counsel).

86/ Sorrell, 679 F.2d at 1327 (citing Quinn & Co., 452 F.2d at 946-47).

87/ See Robert G. Leigh, 50 S.E.C. 189, 194 (1990) (stating that a broker could not rely on a letter from issuer's counsel because the letter in question dealt only with the legality of reissuing the shares to certain persons and not with the legality of sales by those persons). We note further that a transfer agent's willingness to reissue certificates without restrictive legends does not relieve a broker of his obligation to investigate. Id.

transactions were part of an unregistered distribution. Accordingly, those letters would not diminish Price's responsibility to probe the transactions conducted by Geiger and Kaufmann.

VI.

Violations of the Antifraud Provisions

A. On July 30, 1999, Starnet filed with the Commission its annual report on Form 10-KSB for the fiscal year ending April 30, 1999. On August 12, 1999, Starnet filed an amended annual report for fiscal year 1999 on Form 10-KSB/A. In Item 12 of each form, which was required to contain disclosure regarding "Certain Relationships and Related Transactions," Starnet stated that there was "nothing reportable." 88/ Zacharias prepared and signed the Form 10-KSB, and both Zacharias and Carley signed the Form 10-KSB/A.

B. Securities Act Section 17(a), Exchange Act Section 10(b), and Exchange Act Rule 10b-5 proscribe fraudulent conduct. Material misstatements, or omissions necessary to make other statements not misleading, in connection with the offer, sale, or purchase of securities constitute violations of these provisions. 89/ The Division contends that Carley and Zacharias violated these provisions by failing to disclose in Starnet's 1999 annual report the nature and extent of the related-party transactions with respect to its Plans. Regulation S-B requires that small business issuers disclose any transactions with related parties that occurred during the

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88/ Item 404 of Regulation S-B, Certain Relationships and Related Transactions, 17 C.F.R. § 228.404. In general, at the time of the conduct described herein, the Item required that, subject to certain exclusions not relevant here, small business issuers disclose any transactions during the previous two years in which the small business issuer was a party and in which individuals or entities specified in Item 404(a), including directors and executive officers, had a direct or indirect material interest. No information needed to be included for any transaction in which the amount involved did not exceed $60,000.

89/ A fact is material if there is a substantial likelihood that a reasonable investor would have considered the omitted or misstated fact important to his or her investment decision, and disclosure of the omitted or misstated fact would have significantly altered the total mix of information available to the investor. Basic Inc. v. Levinson, 485 U.S. 224, 231-32 (1988); TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976).

To violate Sections 17(a), 10(b) and Rule 10b-5, respondents must act with scienter, the "mental state embracing intent to deceive, manipulate or defraud." Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 n.12 (1976). There is no scienter requirement for violations of Sections 17(a)(2) or 17(a)(3) of the Securities Act; negligence is sufficient. Aaron v. SEC, 446 U.S. 680, 685, 701-02 (1980).

previous two years. 90/ Generally, issuers are required (subject to certain exclusions not relevant here) to disclose transactions in which the issuer was a party, the amount exceeded $60,000, and an executive officer or director (among others) had a direct or indirect material interest in the transaction. 91/

Starnet needed to disclose the transactions which resulted in its directors and executive officers, among others, obtaining cash in the amount that they would have obtained had they been able to exercise their stock options. Item 404 of Regulation S-B required disclosure of the transactions through which Starnet enabled its Option Holders to obtain the financial benefit equivalent to the exercise of those options. The transactions were not simple option exercises and were materially different from the transactions contemplated by Starnet's option plans. Starnet, through Zacharias, devised a procedure to facilitate the exercise of the options. This procedure involved a series of transactions that exceeded $60,000 and that resulted in the Option Holders receiving cash in the amount that they would have obtained had they been able to exercise the options. The Peeper Entities sold shares with the proceeds going to the Option Holders, and the Peeper Entities received the Option Holders' shares as replacements. The fact that Starnet arranged the series of transactions in excess of $60,000 and that the officers and directors had a direct material interest in those transactions required their disclosure under Item 404.

Zacharias argues that the employee stock option transactions in question did not need to be disclosed because the price of the Regulation S stock and prices at which the options and Regulation S warrants were issued had been negotiated at arms-length and determined prior to the time that the option exercise plan was devised. Whether the price of the stock, warrants, and options had been disclosed is not dispositive because Zacharias and Carley failed to disclose the related-party "swap" transactions from which they benefitted. These "swap" transactions were not typical option exercise transactions -- the transactions were not contemplated in, and could not be expected from, the disclosures contained in Starnet's Forms S-8. In reports filed under Section 16 of the Exchange Act, Carley and Zacharias reported sales of Starnet shares obtained upon exercise of options. The funds that Carley and Zacharias received, however, came from the sales of Starnet shares by the Peeper Entities as part of the "swap" transactions outlined above, and not from their own sales of Starnet shares. The reports filed by Carley and Zacharias did not disclose that Carley and Zacharias received funds from the swap transactions involving the Peeper Entities rather than from a standard option exercise. The omitted disclosures were material because they had the effect of hiding the distribution through the Peeper Entities' sales of unregistered Starnet securities to facilitate the exercise of options by Starnet officers in

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90/ Item 404 of Regulation S-B, Certain Relationships and Related Transactions, 17 C.F.R. § 228.404.

91/ Id.

violation of Securities Act Section 5. Thus, the undisclosed sales could expose the company to claims of rescission under Securities Act Section 12. 92/

The record establishes that Carley and Zacharias acted with scienter in failing to disclose as a related-party transaction in Starnet's 1999 annual report the procedure for Starnet officers and employees to exercise their Plan options. Carley and Zacharias each knew that a procedure had been put in place at Starnet to permit them to obtain the cash that they would have received had they been able to exercise their stock options. Zacharias negotiated the structure of the option exercise program with Gould and processed the warrant exercises by Peeper which allowed the program to work. Zacharias testified that he did not take any steps to amend any of the company's public filings to disclose the method by which Starnet officers would resell their Plan Shares. The irrevocable authorizations that Carley and Zacharias signed as part of their exercise of Plan options and resulting sales of Plan Shares informed them that Starnet was "facilitating this trade." It further informed them that shares were being sold "on my behalf" prior to their receipt of the Plan Shares and that they were authorizing Gould to transfer their Plan Shares "into an appropriate account in order to reimburse for the shares sold on my behalf." At a minimum, Carley and Zacharias were reckless in ignoring these numerous indications that, when Starnet arranged for the Peeper Entities to sell Starnet shares and transfer the proceeds from those sales to the Option Holders in the amounts they would have received had they been able to exercise their options, Starnet was participating in a related-party transaction that should have been disclosed. We conclude that Carley and Zacharias violated the antifraud provisions of the federal securities laws when they omitted to disclose as a related-party transaction in Starnet's 1999 annual report the nature and extent of the plan to provide Starnet officers and employees with a way in which to exercise their Plan options. 93/

C. Carley and Zacharias also violated the Commission's reporting requirements by omitting material information from the applicable Starnet reports as described above. Exchange Act Section 13(a) and Rules 13a-1 and 13a-11 thereunder require issuers of securities registered pursuant to Exchange Act Section 12 to file annual and current reports with the Commission. Exchange Act Rule 12b-20 further requires that such reports include any additional material information that is necessary to make the required statements, in light of the circumstances under which they are made, not misleading. Implicit in Section 13(a) and the rules thereunder is the

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92/ 15 U.S.C. § 77l.

93/ The Division also alleged that Zacharias violated Securities Act Section 17(a), Exchange Act Section 10(b), and Exchange Act Rule 10b-5, and that Carley violated Securities Act Sections 17(a)(2) and (3), with respect to a Form 8-K and Form 8-K/A filed with the Commission in December 1998 and March 1999, respectively, that identified the Regulation S purchasers as "seven separate sophisticated foreign investment groups" when, in fact, those groups were all controlled by one individual, Peeper. In light of the record in this case, we do not reach this allegation.

requirement that the reports be accurate. 94/ When Carley and Zacharias omitted the material information described above from the applicable reports filed with the Commission, they violated Exchange Act Section 13(a) and Exchange Act Rules 12b-20, 13a-1, and 13a-11.

VII.

Violation of the Reporting Requirements

A. Zacharias was an officer and director of Starnet until at least August 12, 1999. Zacharias acquired 10,000 shares of Starnet on July 21, 1999. Although the record contains several Forms 3 and 4 filed by Zacharias, it does not contain a Form 4 disclosing the acquisition of these 10,000 shares.

B. Exchange Act Section 16(a) provides, among other requirements, that any person who is an officer or director of an issuer of equity securities registered pursuant to Section 12 of the Exchange Act shall file with the Commission initial statements disclosing the amount of all equity securities of the issuer of which such person is the beneficial owner as well as statements disclosing any changes in such ownership. 95/ Exchange Act Rule 16a-3 provides that statements of changes in beneficial ownership required by Exchange Act Section 16(a) shall be filed on Form 4. 96/ Zacharias failed to make a filing for the July 21, 1999 acquisition. Accordingly, we find that Zacharias violated Exchange Act Section 16(a) and Rule 16a-3 by failing to file a Form 4 disclosing this transaction. 97/

94/ SEC v. Kalvex, Inc., 425 F. Supp. 310, 316 (S.D.N.Y. 1975). Proof of scienter is not required to establish violations of the Commission's reporting provisions. See Savoy Indus., 587 F.2d at 1167; SEC v. Wills, 472 F. Supp. 1250, 1268 (D.D.C. 1978).

95/ 15 U.S.C. § 78p(a). The purpose of Exchange Act Section 16 is to require disclosure of the corporate holdings of, among others, officers and directors of the corporation, as well as prompt disclosure of any changes that occur in their corporate holdings. SEC v. World-Wide Coin Invs., Ltd., 567 F. Supp. 724, 758 (N.D. Ga. 1983). No showing of scienter is required to establish a violation of this provision. Savoy, 587 F.2d at 1167. In 1999, Section 16(a) provided that a statement disclosing a change in the ownership of the issuer's securities be filed within ten days of the close of the calendar month in which the change occurred. 15 U.S.C. § 78p(a) (1994) (amended 2002).

96/ 17 C.F.R. § 240.16a-3.

97/ Although Zacharias contends in his petition for review that "[t]he finding that Mr. Zacharias violated Section 16(a) of the Exchange Act by failing to file a required Form 4 is not supported by substantial evidence in the record taken as a whole," his briefs do not address the law judge's finding that he committed a violation of Section 16(a).

VIII.

A. Severance

Kaufmann argues that his due process rights were violated by our denial of his motion to sever the charges against him from this proceeding. 98/ We denied Kaufmann's motion on the ground that "joinder before the Commission requires only that there be a common issue of law or fact" and the OIP alleged that all the Respondents were involved in a single plan to distribute unregistered securities. 99/ Kaufmann demonstrates no prejudice from this denial. The plan involved facts common to each of the Respondents. The evidence established that Kaufmann was a necessary participant and substantial factor in the execution of the plan. We have evaluated the record with respect to Kaufmann's individual conduct and have assessed his liability and imposed sanctions accordingly.

Price argues that the severance of certain Respondents from this proceeding prejudiced his case. 100/ Mark Dohlen, Starnet's chief executive officer, Paul A. Giles, president and a director of Starnet, and Peeper were each named as Respondents, but were severed from this proceeding because they had not been served with the OIP. The OIP alleged that Price failed reasonably to supervise Spencer Edwards employees Geiger and Kaufmann. Both Geiger and Kaufmann testified at the hearing. Dohlen, Giles, and Peeper were not employed by or associated with Spencer Edwards. While Dohlen, Giles, and Peeper participated in the effort to distribute Starnet shares, there was ample evidence about that plan. Price does not explain how evidence that could be offered by Dohlen, Giles, and Peeper would be relevant to his supervision of Geiger and Kaufmann. 101/

B. Statute of Limitations

Kaufmann claims that the statute of limitations in 28 U.S.C. § 2462, in conjunction with the decision of the United States Court of Appeals for the District of Columbia Circuit in

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98/ See Order Denying Motion of Thomas A. Kaufmann to Sever Proceedings, Exchange Act Rel. No. 50695 (Nov. 18, 2004), 84 SEC Docket 434.

99/ Id. at 434-35 (citing Commission Rule of Practice 201(a), 17 C.F.R. § 201.201(a)).

100/ John A. Carley, Exchange Act Rel. No. 50954 (Jan. 3, 2005), 84 SEC Docket 2317-18.

101/ We find the cases cited by Price in support of his argument inapposite here for the same reasons we found them inapposite in Price's motion opposing the severance. See Carley, 84 SEC Docket at 2318 n.6. We also reject Price's contention that denying his alternative motion to sever him from the proceeding prejudiced his case for the same reasons we find proper the denial of Kaufmann's motion to sever.

Johnson v. SEC, 102/ bars this proceeding. Geiger argues that Section 2462 bars the imposition of a cease-and-desist order, a civil penalty, or a bar from association. Section 2462 provides, in pertinent part, that any "proceeding for the enforcement of any civil fine, penalty, or forfeiture" must be commenced "within five years from the date when the claim first accrued." 103/

The violations in this case occurred between December 1998 and February 2001. We initiated these proceedings on September 1, 2004. A substantial portion of the misconduct thus falls within the limitations period because it occurred after September 1, 1999. Accordingly, Kaufmann and Geiger committed willful violations within the limitations period and the proceeding is not time-barred. 104/ We have not considered misconduct occurring before September 1, 1999, in determining to impose bars or civil penalties, but rather have based these sanctions exclusively on Respondents' conduct during the five-year period preceding issuance of the OIP. 105/ However, we may consider acts outside the limitations period as evidence of a respondent's motive, intent, or knowledge in committing violations within the limitations period. 106/ We have also held that remedial relief such as the imposition of a cease-and-desist order is not barred by the statute of limitations in Section 2462. 107/

Carley, Zacharias, and Geiger all argue that Section 2462 bars us from ordering disgorgement with respect to violations that occurred before September 1, 1999. Section 2462 applies, as noted above, to "any civil fine, penalty, or forfeiture," or, as characterized by the court in Johnson, to "punishment[s] imposed by the government for unlawful or proscribed

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102/ In Johnson, the District of Columbia Circuit Court of Appeals held that Section 2462 applied to Commission administrative proceedings. 87 F.3d 484, 486 (D.C. Cir. 1996).

103/ 28 U.S.C. § 2462.

104/ See Robert W. Armstrong, III, Exchange Act Rel. No. 51920 (June 24, 2005), 85 SEC Docket 3011, 3035-36 (finding that 28 U.S.C. § 2462 did not bar a cease-and-desist and Rule 102(e) proceeding where the violations in the case were ongoing and a substantial portion of the misconduct occurred within the limitations period).

105/ See Edgar B. Alacan, Exchange Act Rel. No. 49970 (July 6, 2004), 83 SEC Docket 842, 868-69 (imposing a bar and civil penalty where certain conduct occurred outside the limitations period because the Commission did not consider conduct occurring more than five years before the issuance date of the OIP in determining to impose those sanctions but rather based those sanctions exclusively on the respondent's conduct during the five-year period preceding the issuance date of the OIP).

106/ See Joseph J. Barbato, 53 S.E.C. 1259, 1278 (1999); Sharon M. Graham, 53 S.E.C. 1072, 1089 n.47 (1998), aff'd, 222 F.3d 994 (D.C. Cir. 2000).

107/ See Herbert Moskowitz, 55 S.E.C. 658, 683 (2002).

conduct." 108/ A disgorgement order, however, is not a punitive measure; it is intended primarily to prevent unjust enrichment. 109/ In Johnson, the court held that Section 2462 would not apply to proceedings for the disgorgement of ill-gotten gains. 110/ The disgorgement orders here are limited to such "wrongfully obtained proceeds." 111/ Accordingly, we reject Respondents' contention that Section 2462 precludes us from ordering disgorgement with respect to violations occurring before September 1, 1999. 112/

108/ Johnson, 87 F.3d at 488 (stating that "a 'penalty,' as the term is used in § 2462, is a form of punishment imposed by the government for unlawful or proscribed conduct").

109/ SEC v. Banner Fund Int'l, 211 F.3d 602, 617 (D.C. Cir. 2000).

110/ 87 F.3d at 491 (stating that "where the effect of the SEC's action is to restore the status quo ante, such as through a proceeding for restitution or disgorgement of ill-gotten profits, § 2462 will not apply"); see also SEC v. Dibella, 409 F. Supp. 2d 122, 127 (D. Conn. 2006) ("Section 2462 does not preclude disgorgement action . . . where the claim seeks to 'deprive []one of wrongfully obtained proceeds.'") (quoting SEC v. Lorin, 869 F. Supp. 1117, 1122 (S.D.N.Y. 1994)).

111/ See infra Section IX.C.

112/ We also reject Carley's and Kaufmann's suggestion that Section 2462 bars the assessment of prejudgment interest at the rates imposed by the law judge because such rates are "punitive." The law judge ordered prejudgment interest calculated at the underpayment rate established under Section 6621(a)(2) of the Internal Revenue Code. See Commission Rule of Practice 600(b), 17 C.F.R. § 201.600(b). The IRS underpayment rate is a non-punitive rate. See SEC v. Falbo, 14 F. Supp. 2d 508, 528 (S.D.N.Y. 1998) (ordering application of the "standard non-punitive rate of interest used in enforcement actions (including those for underpayment of taxes)" in fixing an amount to be disgorged); see also SEC v. Berger, 244 F. Supp. 2d 180, 193 (S.D.N.Y. 2001) (ordering prejudgment interest at the IRS underpayment rate because "the remedial purpose of the statute takes on special importance" in an SEC enforcement action and the underpayment rate "'reflects what it would have cost to borrow the money from the government and therefore reasonably approximates one of the benefits the defendant derived from its fraud'") (citing SEC v. First Jersey Secs., Inc., 101 F.3d 1450, 1476 (2d Cir. 1996)); Rules of Practice, Exchange Act Rel. No. 35833 (June 9, 1995), 59 SEC Docket 1546, 1596 (stating that prejudgment interest is necessary "to effectuate fully the remedial purposes of disgorgement" and that "the IRS underpayment rate is a reasonable and appropriate rate to use in assessing prejudgment interest on disgorgement ordered as the result of remedial administrative proceedings").

IX.

A. Bar Orders

Exchange Act Section 15(b)(6) authorizes the Commission to censure, place limitations on, suspend, or bar a person associated with a broker, dealer, or municipal securities dealer if the Commission finds such sanctions in the public interest and the person has, among other violations, willfully violated the federal securities laws, or failed reasonably to supervise another person who commits such a violation if such other person is subject to his supervision. 113/ When Congress grants an agency the responsibility to impose sanctions to achieve the purposes of a statute, "the relation of remedy to policy is peculiarly a matter for administrative competence." 114/ We have stated that, in determining an appropriate sanction in the public interest, we consider the egregiousness of the defendant's actions, the isolated or recurrent nature of the infraction, the degree of scienter involved, the sincerity of the defendant's assurances against future violations, the defendant's recognition of the wrongful nature of his conduct, and the likelihood that the defendant's occupation will present opportunities for future violations. 115/

Section 5, "the keystone of the Securities Act," "serves to protect the public in the offer and sale of new securities issues" and "set[s] forth basic requirements for the protection of investors." 116/ After September 1, 1999, Geiger and Kaufmann continued their repeated unregistered sales of Starnet stock, worth millions of dollars in the aggregate, in violation of Section 5. 117/ Their central role in the plan to evade the registration requirements of the

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113/ 15 U.S.C. § 78*o*(b)(6), (b)(4)(D)-(E); see also Leslie A. Arouh, Exchange Act Rel. No. 50889 (Dec. 20, 2004), 84 SEC Docket 1880, 1894.

114/ Butz v. Glover Livestock Comm'n Co., Inc., 411 U.S. 182, 185 (1973) (quoting Am. Power Co. v. SEC, 329 U.S. 90, 112 (1946)).

115/ Arouh, 84 SEC Docket at 1894-95; see also Sharon M. Graham, 53 S.E.C. 1072, 1090 n.48 (1998) (quoting Steadman v. SEC, 603 F.2d 1126, 1140 (5th Cir. 1979), aff'd on other grounds, 450 U.S. 91 (1981)), aff'd, 222 F.3d 994 (D.C. Cir. 2000).

116/ Alvin W. Gebhart, Jr. and Donna T. Gebhart, Exchange Act Rel. No. 53136 (Jan. 18, 2006), 87 SEC Docket 437, 468 (citing First Heritage Inv. Co., 51 S.E.C. 953, 959 (1994) and Indep. Sec. Corp., 47 S.E.C. 780, 784 (1982)), appeal filed, No. 06-71201 (9th Cir.).

117/ We noted earlier that, in accordance with 28 U.S.C. § 2462 and Johnson v. SEC, we have not considered misconduct occurring before September 1, 1999, in determining to impose bars or civil penalties, but rather have based these sanctions exclusively on Respondents'

(continued...)

securities laws with respect to these sales renders their violations egregious. 118/ Geiger and Kaufmann ignored numerous red flags suggesting they were facilitating an unlawful distribution by a statutory underwriter. Their failure to conduct a searching inquiry into the origin of the Starnet stock, despite numerous indications that it was part of an unregistered distribution, evinces a disregard for regulatory requirements that calls into serious question their ability to function as securities professionals. Geiger has previously been disciplined for similar violations. 119/ We believe that, after considering the totality of these factors, the public interest requires imposing a bar from association with a broker or dealer on Geiger and Kaufmann. 120/

We have recognized repeatedly the relevance of prior disciplinary history in imposing sanctions. 121/ Geiger's recent disciplinary history supports a bar with no right to reapply. Geiger's continued willful violations of Securities Act Section 5, after being sanctioned for similar conduct with a Peeper-related entity, justify a bar from association with any broker or

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117/ (...continued)
conduct during the five-year period preceding issuance of the OIP. See supra text accompanying note 108.

118/ See Kirby, 79 SEC Docket at 1105 (finding broker's conduct egregious where broker "facilitated a series of transactions that resulted in the distribution of well over a million dollars worth of unregistered securities into the market").

119/ We reject Geiger's contention that his resignation from Spencer Edwards and the age of the misconduct render remedial relief inappropriate because we find these factors outweighed by other considerations. See Robert Bruce Lohmann, Exchange Act Rel. No. 48092 (June 26, 2003), 80 SEC Docket 1790, 1798 (finding that the public interest warranted a bar and a cease-and-desist order because no assurances existed that respondent, who was not currently employed in the securities industry, would not try to reenter the industry and thereafter have the opportunity to commit future violations); Armstrong, 85 SEC Docket at 3040 (finding age of misconduct outweighed by other factors).

120/ See Arouh, 84 SEC Docket at 1895 (imposing bar where respondent committed egregious misconduct, failed to acknowledge the wrongful nature of his conduct, attempted to shift blame to others, and had opportunities to violate the securities laws in the future through his employment in the securities industry).

121/ See, e.g., Consol. Inv. Servs., 52 S.E.C. at 591 (noting that prior disciplinary history evinces whether an applicant's misconduct is isolated, the sincerity of the applicant's assurance that he will not commit future violations, and the egregiousness of the applicant's misconduct).

dealer. 122/ Kaufmann does not share Geiger's disciplinary history. 123/ The record indicates that Kaufmann has not been subject to disciplinary action since 1983. 124/ Kaufmann's lack of a recent disciplinary history leads us to conclude that a bar with a right to reapply in five years is appropriate. 125/

In his discussion of the sanctions imposed by the law judge, Price does not challenge the imposition of a supervisory bar, and we find that this sanction is in the public interest. Price knew that the Peeper Entities' and the Starnet officers' accounts were selling large amounts of Starnet stock into the market. Price also knew that Geiger committed previous securities law violations involving the unregistered sale of securities in an account controlled by Peeper. However, Price conducted no investigation into the source of the stock. He relied on Geiger's and Kaufmann's representations even though he knew Geiger had lied about his previous misconduct. Price's supervisory failures allowed Geiger and Kaufmann to commit repeated securities law violations between September 1999 and February 2001. Accordingly, we find that the public interest warrants barring Price from associating with any broker or dealer in a supervisory capacity.

B. Cease-and-Desist Orders

Securities Act Section 8A(a) and Exchange Act Section 21C authorize the Commission to impose a cease-and-desist order upon any person who "is violating, has violated, or is about to violate" any provision of either of these acts or any rule or regulation thereunder, or against any person who "is, was, or would be a cause of [a] violation" due to an act or omission the person

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122/ See Frank J. Custable, Jr., 51 S.E.C. 855, 863 (1993) (upholding bar in all capacities because "the fact that [respondent] previously engaged in similar misconduct underscores the appropriateness of the sanctions in this case").

123/ The law judge also noted as mitigating evidence that Kaufmann investigated the history of a stock certificate of Starnet's predecessor company, developed a form for Spencer Edwards to use in investigating the history of shares of stock, and questioned a Commission inspector during a routine audit about the Rule 144 transactions.

124/ In 1983, the Securities Division of the Commonwealth of Massachusetts charged Kaufmann with transacting a securities business in Massachusetts without registering as an agent of a broker or dealer. Kaufmann defaulted and was prohibited from transacting a securities business in Massachusetts until properly registered. Kaufmann has been properly registered and in good standing in Massachusetts since 1985.

125/ We hope to impress upon Kaufmann, by virtue of this sanction, the importance of the regulatory requirements he violated and, thereby, help ensure his compliance in the event he is subsequently permitted to return to the industry. Cf. Kirby, 79 SEC Docket at 1106.

"knew or should have known would contribute to such a violation." 126/ In determining whether a cease-and-desist order is an appropriate sanction, we look to whether there is some risk of future violations. 127/ The risk of future violations required to support a cease-and-desist order is significantly less than that required for an injunction. 128/ Our finding that a violation is egregious "raises an inference that it will be repeated." 129/ We also consider whether other factors demonstrate a risk of future violations, but not all factors need to be considered, and no factor is dispositive. Beyond the seriousness of the violation, these factors include the isolated or recurrent nature of the violation, whether the violation is recent, the degree of harm to investors or the marketplace resulting from the violation, the respondent's state of mind, the sincerity of assurances against future violations, recognition of the wrongful nature of the conduct, opportunity to commit future violations, and the remedial function to be served by the cease-and-desist order in the context of any other sanctions sought in the proceeding. 130/

We find that the public interest warrants imposing cease-and-desist orders against Carley and Zacharias. Their failures to disclose material facts in violation of the antifraud provisions and their sales of unregistered securities in violation of the registration requirements constitute serious misconduct. 131/ "[C]onduct that violate[s] the antifraud provisions of the federal securities laws is especially serious and subject to the severest of sanctions under the securities laws." 132/ As noted above, the registration requirements of the federal securities laws are "at the heart of the securities regulatory system" and disregarding those requirements justifies strong remedial measures. 133/ These violations occurred repeatedly over an extended period of

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126/ 15 U.S.C. §§ 77A(a), 78u-3.

127/ KPMG Peat Marwick, LLP, 54 S.E.C. 1135, 1185 (2001), motion for reconsideration denied, 55 S.E.C. 1 (2001), petition denied, 289 F.3d 109 (D.C. Cir. 2002).

128/ KPMG Peat Marwick, 54 S.E.C. at 1191.

129/ See Geiger v. SEC, 363 F.3d 481, 489 (D.C. Cir. 2004).

130/ KPMG Peat Marwick, 54 S.E.C. at 1192.

131/ We specifically reject Carley's characterization of his violations as "at the less-serious end of the spectrum" and "an isolated event."

132/ Gebhart, 87 SEC Docket at 469 (citing Marshall E. Melton, Investment Advisers Act Rel. No. 2151 (July 25, 2003), 80 SEC Docket 2812, 2825).

133/ Kirby, 79 SEC Docket at 1105.

time. 134/ Zacharias will have opportunities to commit future violations in his role as a consultant assisting firms in rasing capital by issuing securities, and Carley, although not currently employed by an issuer, may again become active in the financial markets at any time. In his brief, Carley argues that imposition of sanctions "would impair [his] ability to serve as an officer or director of a public company," suggesting that he will seek such opportunities in the future. 135/ A cease-and-desist order will serve the remedial purpose of encouraging both Respondents to take their responsibilities more seriously in the future. We find that the serious and prolonged nature of the violations establishes a sufficient risk of future violations warranting cease-and-desist orders against Carley and Zacharias. 136/

We reject Zacharias's contention that cease-and-desist relief against him is inappropriate because he "had a reasonable belief in the propriety of his actions." 137/ Zacharias failed to take basic precautions to ensure that Starnet did not violate the federal securities laws. Zacharias did not obtain a legal opinion regarding the propriety of the plan that enabled Starnet's officers and employees to exercise their stock options and sell their stock. He also took no steps to amend

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134/ We consider the entire record here because the statute of limitations in 28 U.S.C. § 2462 does not apply to cease-and-desist proceedings. See supra text accompanying note 107.

135/ Carley cites SEC v. First City Fin. Corp., 890 F.2d 1215, 1229 (D.C. Cir. 1989), for the proposition that the law judge improperly "held it against" Carley that Carley "offered no assurances against future violations or recognized the wrongful nature of his conduct." However, in Geiger v. SEC, the court specifically rejected the argument Carley advances here. Geiger, 363 F.3d at 489.

136/ Carley contends that the age of the misconduct militates against imposing a cease-and-desist order, but the other relevant factors more than justify cease-and-desist relief. Cf. Armstrong, 85 SEC Docket at 3040 (finding age of misconduct outweighed by other factors).

137/ To the extent Zacharias relies on any assurances from Brovarone, we find such reliance unavailing. Brovarone testified that he represented Peeper and the entities purchasing the Regulation S stock. One cannot rely on the advice of another's counsel because that counsel cannot be relied upon to give disinterested advice. Sorrell v. SEC, 679 F.2d 1323, 1327 (9th Cir. 1982) ("A broker may not rely on counsel's advice when the attorney is an interested party."); C.E. Carlson, Inc. v. SEC, 859 F.2d 1429, 1436 (10th Cir. 1988) ("We agree with SEC that counsel also must be independent."); David M. Haber, 52 S.E.C. 201, 206 (1995) ("However, Haber could not rely on counsel for Brown, who could not be counted on to give disinterested advice.").

any of the company's public filings to disclose this plan. In our view, Zacharias's insistence that he behaved reasonably in light of this evidence suggests the need for cease-and-desist relief. 138/

We also find that the public interest warrants imposing cease-and-desist orders against Geiger and Kaufmann. In addition to the factors discussed above with respect to imposing a bar, Geiger and Kaufmann pose a risk of future violations. Geiger's serious and repeated misconduct over an extended period, along with his disciplinary history, raises at least "some risk" of future violations. 139/ Whether or not Kaufmann seeks association in the securities industry after five years, a cease-and-desist order will serve the remedial purpose of encouraging him to take his responsibilities and the securities registration requirements more seriously. Given the seriousness of their violations and their apparent failure to appreciate their duties as securities professionals, we find that the record presents sufficient risk that Kaufmann and Geiger will commit future violations to warrant imposition of cease-and-desist orders.

C. Disgorgement

Exchange Act Section 21B authorizes orders of disgorgement in, among others, cases involving willful violations of the Securities Act or the Exchange Act. 140/ Disgorgement is an equitable remedy designed to deprive wrongdoers of unjust enrichment and to deter others from violating the securities laws. 141/ Disgorgement need only be a reasonable approximation of profits causally connected to the violation. 142/ Once the Division establishes that its disgorgement figure reasonably approximates the amount of unjust enrichment, the burden of going forward shifts to the Respondents who are "then obliged clearly to demonstrate that the

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138/ We have determined in our discretion not to impose a cease-and-desist order on Zacharias with respect to Exchange Act Section 16(a) and Exchange Act Rule 16a-3.

139/ See Mark David Anderson, Exchange Act Rel. No. 48352 (Aug. 15, 2003), 80 SEC Docket 3250, 3271 (imposing cease-and-desist order where respondent's "serious and repeated misconduct over an extended period, along with his disciplinary history, raise[d] at least 'some risk' of future violations"); Kenneth R. Ward, Exchange Act Rel No. 47535 (Mar. 19, 2003), 79 SEC Docket 3035, 3062 (finding that respondent's "serious misconduct and disciplinary history raise[d] at least 'some risk' of future violations"), aff'd, 75 Fed. Appx. 320 (5th Cir. 2003).

140/ 15 U.S.C. § 78u-2(e).

141/ First City Fin. Corp., 890 F.2d at 1230; SEC v. Johnston, 143 F.3d 260, 263 (6th Cir. 1998); John J. Kenny, Exchange Act Rel. No. 47847 (May 14, 2003), 80 SEC Docket 564, 595, aff'd, 87 Fed. Appx. 608 (8th Cir. 2004).

142/ First City Fin. Corp., 890 F.2d at 1231; see also SEC v. Bilzerian, 29 F.3d 689, 697 (D.C. Cir. 1994).

disgorgement figure was not a reasonable approximation." 143/ Where disgorgement cannot be exact, "any risk of uncertainty . . . should fall on the wrongdoer whose illegal conduct created that uncertainty." 144/

The Division has established that, in connection with the sale of unregistered Starnet stock, Carley received $2,489,740 through his United Capital account. Carley argues that ordering him to disgorge this amount would be punitive because he would owe nothing if "the securities professionals relied upon by Mr. Carley had done their jobs right" and because he "was not the cause of the damage the [Commission] seeks to remedy through disgorgement." Carley, however, was a necessary participant in the unregistered sale of Starnet stock in violation of the federal securities laws, and he profited from these transactions. The amounts Carley received through these sales are therefore ill-gotten gains that should be disgorged. 145/

The Division has established that Zacharias received $1,451,128.55 through his United Capital account in connection with the sale of unregistered Starnet stock. Zacharias argues that disgorgement of this amount would be punitive because such disgorgement would not "return Mr. Zacharias to the status quo ante" as "[r]eturning Mr. Zacharias to the status quo ante would require restoration" of his Starnet stock. Zacharias sold that stock, however, in violation of Section 5 of the Securities Act. Disgorgement prevents Zacharias from retaining the proceeds of these illegal sales and as such serves a remedial rather than punitive purpose. 146/ Zacharias also

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143/ First City Fin. Corp., 890 F.2d at 1232.

144/ SEC v. Patel, 61 F.3d 137, 140 (2d Cir. 1995).

145/ See SEC v. Gemstar-TV Guide Inter., Inc., 401 F.3d 1031, 1047 (9th Cir. 2005) ("The deterrent effect of a Commission enforcement action would be greatly undermined if securities law violators were not required to disgorge illicit profits."), cert. denied, 126 S. Ct. 416 (2005).

The Division also seeks an order requiring Carley to disgorge the $1,687,578.38 that Madison Park Trust received from the sale of Starnet stock. We have determined not to impose such an order in light of our conclusion dismissing the allegations with respect to sales by Madison Park Trust.

146/ See Gartner v. SEC, 913 F. Supp. 1372, 1377 n.6 (C.D. Cal. 1995) (stating that an "SEC disgorgement proceeding serves a remedial purpose by divesting a violator of the securities laws of ill-gotten gains"); see also SEC v. ETS Payphones, Inc., 408 F.3d 727, 735 (11th Cir. 2005) (stating that the purpose of disgorgement is to deprive the wrongdoer of his ill-gotten gain); SEC v. Randy, 38 F. Supp. 2d 657, 673-74 (N.D. Ill. 1999) (stating that the Seventh Circuit "has explained that disgorgement is a remedial

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argues that disgorgement is not appropriate because it will not serve to reimburse persons who suffered losses by his conduct. The remedy of disgorgement, however, is designed primarily to deprive wrongdoers of their ill-gotten gains, not to compensate for damages, if any, suffered by the victims of the wrongful conduct. 147/

The Division has presented a summary of evidence from Spencer Edwards's clearing firm detailing the commissions generated by transactions in Starnet stock in the customer accounts of Kaufmann and Geiger from January 1999 through February 2001. In determining the amount of disgorgement sought from Kaufmann and Geiger, the Division excluded commissions generated on sale transactions by persons "unrelated" to Respondents. 148/ The Division assumed, based on Kaufmann's investigative testimony, that Spencer Edwards retained thirty percent of the gross commission generated by Kaufmann's and Geiger's client accounts. With respect to the remaining seventy percent, the law judge concluded that Kaufmann and Geiger split the commissions generated from trades made under their joint account number on an equal basis and ordered Kaufmann and Geiger each to disgorge $885,738.62.

Kaufmann asserts a variety of sometimes conflicting reasons that he argues support his claim that he should not have to disgorge half of the gross profits generated by trades under his and Geiger's joint account number. Kaufmann argues that he executed trades only for Starnet officers, while Geiger executed trades for the Peeper Entities. Kaufmann claims that commissions for transactions with respect to their joint account number were allocated based on who generated the business, but also claims that an unsigned handwritten document reflects his agreement with Geiger to divide commissions on a sliding scale based on the amount of commissions earned. In his brief, Kaufmann claims that Geiger's share of commission on the Peeper accounts was seventy-six percent, but Kaufmann and Geiger asserted at the hearing that they split commissions on a sliding scale that varied from month to month.

We are not persuaded by Kaufmann's attempts to reduce the disgorgement amount attributable to him. The law judge found that Kaufmann's and Geiger's testimony regarding the

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146/ (...continued)
measure to deter future violations of the securities laws and to deprive wrongdoers of their ill-gotten gains and is not a punitive measure").

147/ First City Fin. Corp., 890 F.2d at 1230; Hately v. SEC, 8 F.3d 653, 655 (9th Cir. 1993).

148/ The Division included in its request for disgorgement commissions on all buy transactions because it was reasonable to infer that purchases of Starnet stock by customers of Kaufmann and Geiger were filled with the substantial inventory of unregistered stock being sold through Spencer Edwards as part of the unregistered distribution. The Division included sale transactions only for Respondents and persons "related" to Respondents.

sliding scale of commissions lacked credibility. 149/ His finding is supported by the numerous and conflicting explanations offered by Kaufmann, which indicate post hoc attempts to limit the disgorgement amount rather than a contemporaneous agreement on splitting commissions. The unsigned, handwritten document contains a chart but no explanation of how it applies or to what accounts it applies. The document is dated July 7, 1999, approximately seven months after the unregistered distribution of Starnet shares began, indicating at a minimum that it did not apply to a significant portion of the trading period at issue here. Given these facts, we find that Kaufmann has failed clearly to demonstrate that the disgorgement sought here was not a reasonable approximation of his ill-gotten gains.

We find Respondents' arguments challenging the disgorgement sought here to be without merit. Ordering disgorgement will prevent the Respondents from reaping substantial financial gain from their violations. Disgorgement will also impress upon them and other officers of public companies and associated persons of broker-dealers the need to comply with the registration requirements of the federal securities laws and deter them from evading such requirements in the future in the hopes of reaping a substantial financial windfall. In light of our determination to dismiss the allegations with respect to sales by Madison Park Trust, we will not order disgorgement with respect to commissions obtained from those sales and, therefore, we will reduce the disgorgement amount ordered against both Kaufmann and Geiger by $12,591.78. Accordingly, we order Carley to disgorge $2,489,740, Zacharias to disgorge $1,451,128.55, and Kaufmann and Geiger each to disgorge $873,146.84. 150/

D. Civil Money Penalties

Exchange Act Section 21B authorizes the Commission to impose a civil penalty in any proceeding instituted pursuant to, among other provisions, Exchange Act Sections 15(b)(4) and 15(b)(6) where the Commission finds that such penalty is in the public interest and that a respondent has, among other misconduct, willfully violated any provision of the federal securities

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149/ Tricarico, 51 S.E.C. at 460 (stating that credibility findings are entitled to "considerable weight" and "can be overcome only where the record contains 'substantial evidence' for doing so").

150/ Securities Act Section 8A(e) and Exchange Act Sections 21B(e) and 21C(e) authorize the Commission to assess "reasonable interest" in connection with an order for disgorgement in any cease-and-desist proceeding or any proceeding in which a civil money penalty could be imposed. Commission Rule of Practice 600(b) provides that interest shall be computed at the underpayment rate established by Section 6621(a)(2) of the Internal Revenue Code and shall be compounded quarterly. We have held previously that the IRS underpayment rate applies to disgorgement amounts for the entire period from the date of assessment until paid. Alacan, 83 SEC Docket at 872 n.79 (citing Laurie Jones Canady, 54 S.E.C. 65, 85 (1999)). The Division contends that the starting date for the assessment of prejudgment interest should be March 1, 2001.

laws or failed reasonably to supervise another person who has committed such violations. 151/ Section 21B establishes three tiers of penalties, each with a larger maximum penalty amount, applicable to increasingly serious misconduct. 152/ The factors we consider in assessing the penalty required in the public interest are whether there was fraudulent misconduct, harm to others, or unjust enrichment, whether the respondents had prior violations, and the need for deterrence, as well as such other matters as justice may require. 153/ The law judge imposed third-tier penalties of $400,000 on Geiger and $300,000 on Kaufmann. The law judge imposed a second-tier penalty of $150,000 on Price.

We find third-tier penalties appropriate in response to Geiger's and Kaufmann's misconduct. The Exchange Act provides that we may impose third-tier penalties where 1) the misconduct "involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement"; and 2) such misconduct "directly or indirectly resulted in substantial losses or created a significant risk of substantial losses to other persons or resulted in substantial pecuniary gain to the person who committed" the misconduct. 154/ Geiger's and Kaufmann's misconduct involved both a reckless disregard of the registration requirements of the federal securities laws and substantial pecuniary gain to themselves.

The maximum third-tier penalty for misconduct by a natural person committed during the time period at issue in this proceeding was $110,000 for each violation. 155/ We have determined to impose civil penalties based on the totality of Geiger's and Kaufmann's misconduct. Both Geiger and Kaufmann participated in an unlawful distribution. They executed the trades that effectuated the unregistered sales of Starnet stock into the market. They followed Gould's instructions regarding the sales of Starnet stock and the distribution of the proceeds. Geiger handled the trades in the Peeper entities' accounts and Kaufmann handled the trades in the Starnet officers' Spencer Edwards accounts. Geiger and Kaufmann enriched themselves through this substantial participation in the offer and sale of unregistered securities. Significant penalties are necessary to deter other violators. 156/ Some of the conduct in question occurred

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151/ 15 U.S.C. § 78u-2.

152/ Id. § 78u-2(b).

153/ See, e.g., William C. Piontek, Exchange Act Rel. No. 48903 (Dec. 11, 2003), 81 SEC Docket 3044, 3060.

154/ 15 U.S.C. § 78u-2(b)(3).

155/ 17 C.F.R. § 201.1001.

156/ We reject Kaufmann's argument that a civil penalty is inappropriate because there is no reasonable basis that the penalty will remedy the harm caused by Kaufmann's

(continued...)

outside of the limitations period, and we consider this fact in reducing the penalty imposed by the law judge. Nevertheless, Kaufmann's and Geiger's large number of sales of unregistered Starnet stock after September 1, 1999, violated Section 5, and they each received substantial gains from these violative sales. Accordingly, we impose one third-tier penalty of $110,000 each on Geiger and Kaufmann. 157/

We find a second-tier penalty appropriate in response to Price's failure to supervise. The Exchange Act provides that we may impose second-tier penalties where the misconduct "involved fraud, deceit, manipulation, or deliberate or reckless disregard of regulatory requirement." 158/ Price's failure to supervise involved a reckless disregard for his supervisory responsibilities in light of the numerous red flags suggesting that Geiger and Kaufmann were violating the securities laws.

The maximum second-tier penalty for misconduct by a natural person committed during the time period at issue in this proceeding was $55,000 for each violation. 159/ Price's supervisory failures allowed Geiger and Kaufmann unjustly to enrich themselves. Price has no disciplinary history, but he failed to supervise Geiger reasonably despite his knowledge that Geiger committed previous misconduct involving violations of the same provisions Geiger violated here. As demonstrated above, Price's supervision of Geiger and Kaufmann approached

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156/ (...continued)
misconduct. A civil money penalty is designed to serve as a deterrent against securities law violations. SEC v. Lybrand, 281 F. Supp. 2d 726, 729 (S.D.N.Y. 2003).

157/ We have previously considered each violative action as deserving of a separate penalty. See Anderson, 80 SEC Docket at 3270. To help place these sanctions in context, we note that each of the numerous unregistered sales of Starnet stock that took place after September 1, 1999, could be considered a separate violation of Securities Act Section 5. We believe, based on the facts and circumstances of this case, that imposing one third-tier penalty is appropriate.

158/ 15 U.S.C. § 78u-2(b)(2).

159/ 17 C.F.R. § 201.1001.

willful blindness. Accordingly, we find a civil money penalty of $55,000 – one maximum second-tier penalty – appropriate in the public interest. 160/

An appropriate order will issue. 161/

By the Commission (Chairman COX and Commissioners ATKINS, NAZARETH, and CASEY).

Nancy M. Morris
Secretary

160/ Price asserts an inability to pay civil penalties. The law judge determined that Price had the ability to pay a civil penalty of $150,000, representing 16% of his reported net worth. Price contends that the law judge improperly included his pension assets and the value of his home in making this determination. Although Price submitted a sworn financial statement to the law judge, he did not comply with Commission Rule of Practice 410(c), 17 C.F.R. § 201.410(c), requiring any person seeking review of an initial decision who asserts inability to pay to file with the opening brief a sworn financial statement. We have reduced the penalty imposed by the law judge from $150,000 to $55,000. Under these circumstances, no further reduction is warranted based on an inability to pay. Cf. SEC v. Pardue, 367 F. Supp. 2d 773, 778 (E.D. Pa. 2005) (imposing penalty of $25,000 on defendant with negative net worth of between $50,000 and $100,000); see also SEC v. Svoboda, 409 F. Supp. 2d 331, 348-49 (S.D.N.Y. 2006) (imposing penalty of $150,000 on defendant who represented that his sole remaining asset was an IRA worth $690,000 and penalty of $250,000 on defendant who represented his net worth was $45,450).

161/ We have considered all of the parties' contentions. We have rejected or sustained them to the extent that they are inconsistent or in accord with the views expressed herein.

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Rel. No. 8888 / January 31, 2008

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 57246 / January 31, 2008

Admin. Proc. File No. 3-11626

In the Matter of

JOHN A. CARLEY,
EUGENE C. GEIGER,
THOMAS A. KAUFMANN,
EDWARD H. PRICE, and
CHRISTOPHER H. ZACHARIAS

ORDER IMPOSING REMEDIAL SANCTIONS

On the basis of the Commission's opinion issued this day it is

ORDERED that John A. Carley cease and desist from committing or being a cause of any violations or future violations of Sections 5(a), 5(c), and 17(a) of the Securities Act of 1933, Section 10(b) and 13(a) of the Securities Exchange Act of 1934, and Exchange Act Rules 10b-5, 12b-20, 13a-1, and 13a-11; and it is further

ORDERED that Christopher H. Zacharias cease and desist from committing or being a cause of any violations or future violations of Sections 5(a), 5(c), and 17(a) of the Securities Act of 1933, Section 10(b) and 13(a) of the Securities Exchange Act of 1934, and Exchange Act Rules 10b-5, 12b-20, 13a-1, and 13a-11; and it is further

ORDERED that Eugene C. Geiger and Thomas E. Kaufmann cease and desist from committing or being a cause of any violations or future violations of Sections 5(a) and 5(c) of the Securities Act of 1933; and it is further

ORDERED that Eugene C. Geiger be, and he hereby is, barred from association with any broker or dealer; and it is further

ORDERED that Thomas E. Kaufmann be, and he hereby is, barred from association with any broker or dealer, provided that he may apply to become so associated after five years; and it is further

ORDERED that Edward H. Price be, and he hereby is, barred from association with any broker or dealer in a supervisory capacity; and it is further

ORDERED that John A. Carley disgorge $2,489,740.00, plus prejudgment interest of $1,296,061.63, Christopher H. Zacharias disgorge $1,451,128.55, plus prejudgment interest of $755,401.00, Eugene C. Geiger disgorge $873,146.84, plus prejudgment interest of $454,526.24, and Thomas A. Kaufmann disgorge $873,146.84, plus prejudgment interest of $454,526.24, such prejudgment interest calculated beginning on March 1, 2001, in accordance with Commission Rule of Practice 600; and it is further

ORDERED that Eugene C. Geiger pay a civil money penalty of $110,000, Thomas A. Kaufmann pay a civil money penalty of $110,000, and Edward H. Price pay a civil money penalty of $55,000;

Payment of the amount to be disgorged and the civil money penalty shall be: (i) made by United States postal money order, certified check, bank cashier's check, or bank money order; (ii) made payable to the Securities and Exchange Commission; (iii) mailed or delivered by hand to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Alexandria, Virginia 22312; and (iv) submitted under cover letter that identifies the Respondent and the file number of this proceeding. A copy of the cover letter and check shall be sent to Julie K. Lutz, counsel for the Division of Enforcement, Securities and Exchange Commission, 1801 California Street, Suite 1500, Denver, Colorado 80202.

By the Commission.

Nancy M. Morris
Secretary