

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

June 8, 2004

ADMINISTRATIVE PROCEEDING
File No. 3-11515

In the Matter of

CHARLES W. CROUSE and
NORMAN R. HESS,

Respondents.

ORDER INSTITUTING
ADMINISTRATIVE AND CEASE-AND-
DESIST PROCEEDINGS PURSUANT
TO SECTION 8A OF THE SECURITIES
ACT OF 1933 AND SECTIONS 15(b)
AND 21C OF THE SECURITIES
EXCHANGE ACT OF 1934

I.

The Securities and Exchange Commission (“Commission”) deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 8A of the Securities Act of 1933 (“Securities Act”) and Sections 15(b) and 21C of the Securities Exchange Act of 1934 (“Exchange Act”) against Charles W. Crouse (“Crouse”) and Norman R. Hess (“Hess”) (collectively referred to as “Respondents.”).

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. Crouse, 43, resides in Marietta, Georgia. He has been a registered representative since May 1992. During the time period of the events discussed herein, Crouse was a registered representative at a broker-dealer (the “Broker-Dealer”) and holds Series 7 and 63 securities licenses. Crouse left the Broker-Dealer in March 2001 and is currently associated with another broker-dealer.

2. Hess, 67, resides in Atlanta, Georgia. Hess was president of the Broker-Dealer from 1994 through July 2000 and had overall responsibility for compliance and supervision at the firm. Hess holds Series 7, 8, 23, 27 and 63 securities licenses and has over thirty years of experience in the brokerage industry working at many large brokerage firms.

Hess voluntarily left the Broker-Dealer in March 2001 and is currently employed at another brokerage firm.

B. MARK DRUCKER'S PONZI SCHEME

1. In December 1997, Mark Drucker ("Drucker") opened a brokerage account ("the Account") at the Broker-Dealer. His registered representative at the Broker-Dealer was Crouse. During the relevant period, Drucker operated a Ponzi scheme in which he deposited approximately \$6.3 million of investor funds into the Account.

2. From at least June 1998 through September 1999, Drucker obtained funds from investors by representing that he would use their funds to buy and sell securities through an account at the Broker-Dealer in his name and under his management. Drucker's investment strategy consisted of day-trading options and equities in the Account using a momentum computer program. Drucker told Crouse that he was a dot.com millionaire who had sold "something to NASA" and had sold a product or concept to Microsoft Corporation.

3. Most of Drucker's investors signed management agreements provided by Drucker allowing him to have "full and complete discretion to invest, trade and make transactions associated with the Account." While the terms of the investments varied from investor to investor, in most cases, Drucker promised guaranteed returns of up to fifty percent (50%) in ninety days or less. In some instances, Drucker provided investors with agreements rolling over the original investment and purported profit. These agreements indicated a higher value of their investments than actually existed.

4. Contrary to his representations to investors, Drucker was consistently losing money from his trading. For the thirteen-month period from December 2, 1997 through December 31, 1998, Drucker lost \$225,660 in the Account.

5. Drucker's trading, and his trading losses, increased substantially in 1999. For the nine-month period from January 1, 1999 through September 30, 1999, net losses in the Account amounted to \$634,453. With the exceptions of January and March, the Account lost money every month in 1999.

6. Drucker's trading program was a Ponzi scheme. Drucker's payments to investors were funded from deposits into the Account that came from new investors. Drucker was dependent on money from new investors to keep his scheme operating.

C. CROUSE'S ASSISTANCE IN FURTHERANCE OF DRUCKER'S PONZI SCHEME

1. Crouse knew, among other things, of the Account's high activity level and substantial losses. He also knew or was reckless in not knowing that almost all the money deposited into the Account was coming from checks written by other people to Drucker because he received copies of all checks deposited into the Drucker Account. Twenty of these checks, totaling in excess of \$500,000, specifically had references to either a "loan," "investment,"

“p’pship invest,” “stock,” or “agreement.” Crouse also knew that Drucker wrote checks out of the Account to some of the same persons whose checks had been previously deposited into the Account despite massive losses. Crouse also knew that Drucker was managing the accounts of other Broker-Dealer customers and that he had lost large amounts of money in some of those accounts as well. Additionally, Crouse received letters from two of his other customer accounts at the Broker-Dealer in June 1999 telling him to transfer money into the Account; one letter stated “He [Drucker] will manage this money from his account.” During that same week, Crouse assisted Drucker in convincing two people to invest money in the Account. Taken together these facts showed a scheme by Drucker to defraud investors that Crouse facilitated by either knowing and permitting it or actively assisting in it.

2. Crouse substantially assisted Drucker in furtherance of his Ponzi scheme by executing all trades in the Account and assisting Drucker in convincing at least two investors to invest in the Account. Crouse knew or was reckless in not knowing that Drucker, his largest customer, was operating a Ponzi scheme out of the Account.

D. HESS’S FAILURE TO SUPERVISE CROUSE

1. Hess was the Broker-Dealer’s President and General Securities Principal. He was also the immediate and only supervisor of Crouse. The Broker-Dealer’s Supervisory Procedures and Compliance Manual states that the “General Securities Principal” is responsible “for the supervision of all general securities representatives and their activities” and “for the daily review of order tickets and quarterly review of all trading activity.”

2. Hess reviewed exception reports, which flagged the high level of trading in the Account, and signed five “active account” letters sent to Drucker regarding the activity in the Account. Hess also examined the Account’s order tickets on a daily basis, reviewed Crouse’s commission runs on a monthly basis and active account compliance reports at least three times a year. As a result of this review, Hess was aware of the Account’s large losses.

3. In accordance with firm procedure, Hess reviewed monthly statements that showed checks were being paid to third parties who had previously put money into the Account despite massive losses. As Crouse’s immediate and direct supervisor, Hess was responsible for conducting further investigation into whether Crouse was facilitating a violation of the securities laws. Hess did not discharge his supervisory duties and failed to investigate these “red flags.”

4. Commissions from the Account were approximately eight percent of the total commissions received by the Broker-Dealer during the period from October 1998 to September 1999. During this time, the Broker-Dealer served between 2,800 and 3,000 accounts. Commissions from the Account during this time amounted to one-third of Crouse’s income from the Broker-Dealer. Hess also knew that the Account was the Broker-Dealer’s most active during the relevant time period. During its existence, Hess received an override on the Account of \$5,828

5. Although Hess was aware of the Account’s heavy trading, large losses and large commissions and knew or was reckless in not knowing of the third-party checks deposited into the Account, the funds provided to Drucker by third parties for deposit into the Account as well as

checks issued out of the Account to third parties who had previously deposited money into the Account despite massive losses, he did not investigate Crouse's conduct or take any reasonable steps to determine whether any illegal activity was occurring in the Account.

6. In addition, as president of the Broker-Dealer, Hess was ultimately and solely responsible for establishing supervisory procedures and a system to effectively implement those procedures. Hess failed to establish a system for implementing the Broker-Dealer's procedures that called for review of (a) incoming customer correspondence regarding customer accounts; and (b) review and approval of third-party checks for deposit into accounts.

7. Because Hess failed to establish a system to implement these procedures, Hess and others at the Broker-Dealer failed to detect a pattern of unusual deposits and other unusual activity such as (a) that virtually none of the deposits into the Account were Drucker's money; (b) that several third-party checks were deposited into the Account without appropriate approval as required by the Broker-Dealer's policies and procedures; (c) that numerous checks containing notations such as "loan," "investment," "stock" or "agreement" were deposited into the Account; and (d) that Drucker wrote a number of checks from the Account to third parties who previously had written checks that were deposited into the Account despite massive losses. In addition, Hess failed to take action despite the Broker-Dealer receiving, during the first week of June 1999, correspondence from two of its customers instructing the firm to transfer all assets in their accounts at the Broker-Dealer to the Account. One of the letters stated that the purpose of the transfer was to have Drucker manage the customer's funds. Had Hess implemented an adequate system to review this correspondence, in light of other red flags concerning this Account, this suspicious pattern of activity could have been detected and follow up taken, to uncover Drucker's Ponzi scheme and Crouse's facilitation of such scheme.

8. Had Hess ensured that the Broker-Dealer had a system in place to detect and take follow-up action in these areas, he could have detected and prevented violations of the securities laws. Hess's supervision was deficient as the Broker-Dealer's supervisory procedures did not provide for a meaningful review of records that would have alerted Hess and the Broker-Dealer to potential violations of the securities laws. Because Hess and the Broker-Dealer failed to establish adequate procedures and a system to implement these procedures, requiring an effective review of these records and/or an effective system to investigate and address the results of such a review, Hess and the Broker-Dealer failed to detect that Crouse was facilitating Drucker's violation of the securities laws.

9. Hess did not reasonably delegate responsibility for seeing that the Broker-Dealer's procedures were implemented. As president of the Broker-Dealer, Hess was responsible for ensuring that the firm had a system in place to implement procedures and that all the procedures were followed unless and until he reasonably delegated particular functions to another person in the Broker-Dealer, and neither knew nor had reason to know that such person's performance was deficient. Consol. Inv. Serv., Inc., 1994 SEC LEXIS 4045 (Dec. 12, 1994) initial decision has become final, 52 S.E.C. 582 (1996). Hess never delegated supervisory responsibility to see that compliance procedures were implemented.

E. VIOLATIONS

As a result of the conduct described above, Crouse willfully aided and abetted and caused Drucker's violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, which prohibit fraudulent conduct in the offer and sale of securities and in connection with the purchase or sale of securities.

As a result of the conduct described above, Hess failed reasonably to supervise Crouse, within the meaning of Section 15(b)(4)(E) of the Exchange Act, with a view toward preventing his willful aiding and abetting violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate in the public interest that public administrative and cease-and-desist proceedings be instituted to determine:

A. Whether the allegations set forth in Section II above are true and, in connection therewith, to accord Respondents with the opportunity to establish defenses to such allegations;

B. What, if any, remedial action is appropriate in the public interest against Respondents pursuant to Section 8A of the Securities Act and Section 15(b) of the Exchange Act including, but not limited to, disgorgement and civil penalties pursuant to Section 21C of the Exchange Act; and

C. Whether, pursuant to Section 8A of the Securities Act and Section 21C of the Exchange Act, Crouse should be ordered to cease and desist from committing or causing violations of and any future violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

IV.

IT IS ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened not earlier than 30 days and not later than 60 days from service of this Order at a time and place to be fixed and before an Administrative Law Judge to be designated by further order as provided by Rule 200 of the Commission's Rules of Practice, 17 C.F.R.

IT IS FURTHER ORDERED that Respondents shall file an Answer to the allegations contained in this Order within twenty (20) days after service of this Order, as provided by Rule 220 of the Commission's Rules of Practice, 17 C.F.R. § 201.220.

If either Crouse or Hess fails to file an answer, or fails to appear at a hearing after being duly notified, they may be deemed in default and the proceedings may be determined against them upon consideration of this Order, the allegations of which may be deemed to be true as

provided by Rules 155(a), 220(f), 221(f) and 310 of the Commission's Rules of Practice, 17 C.F.R. §§ 201.155(a), 201.220(f), 221(f) and 201.310.

This Order shall be served upon Respondents personally or by certified mail.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 300 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice.

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision upon this matter, except as witness or counsel in proceedings held pursuant to notice. Since this proceeding is not "rule making" within the meaning of Section 551 of the Administrative Procedure Act, it is not deemed to be subject to the provisions of Section 553 delaying the effective date of any final Commission action.

By the Commission.

Jonathan G. Katz
Secretary