[COMMITTEE PRINT]

THE PENN CENTRAL FAILURE AND THE ROLE OF FINANCIAL INSTITUTIONS

PART III

PENPHIL: THE MISUSE OF CORPORATE POWER

STAFF REPORT OF THE COMMITTEE ON BANKING AND CURRENCY HOUSE OF REPRESENTATIVES

92d Congress, First Session

FEBRUARY 15, 1971

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LETTER OF TRANSMITTAL

FEBRUARY 15, 1971.

To the Members of the House Committee on Banking and Currency:

Transmitted herewith for use of the Banking and Currency Committee and the Congress is Part III of the staff report on *The Penn Central Failure and the Role of Financial Institutions.*

Part III constitutes a classic example of the use of corporate power for personal profit. In effect, it is the chronicle of how two men, David C. Bevan, the former chief financial officer of the Penn Central, and Charles J. Hodge, the former chief investment advisor of the Railroad, manipulated the financial resources, the assets and the credit of the nation's sixth largest corporation for the benefit of an investment company, Penphil, which they established and directed. The ultimate goal of Bevan and Hodge was to create a large conglomerate operating and holding company while orchestrating Penn Central investments in a way that would serve the interests of Penphil. In an overall sense, the history of Penphil is not only the story of monumental disservice to the Penn Central, the nation's largest transportation system; it is a detailed record of activities which distorts the concept of the democratic free enterprise system.

The key factors which made the establishment and growth of Penphil possible were the unrestricted line of credit provided Penphil by the Chemical Bank New York Trust Company—a line of credit that was based primarily on the large loan and deposit accounts maintained in the bank by the Penn Central—and the manipulation of Penn Central investments by Bevan and Hodge. In this connection, Penphil's ability to control corporations in which it held common investments with the Penn Central was enhanced by the fact that the membership of Penphil included some of the chief officers of these corporations.

Chemical bank loans to Penphil were made on such favorable terms that they played a large role in enabling most Penphil members to claim a profit of $83,500 on a cash investment of $16,500. Moreover, Chemical extended its million dollar line of credit to Penphil without any regard for the fact that the company's investments placed David Bevan and other Penn Central officials in basic conflict-of-interest situations. This is so, even though Bevan, at one point, openly acknowledged that a conflict-of-interest may have existed regarding Penphil's investments in the Great Southwest Corporation, which is controlled by the Penn Central. Indeed, it is because of Chemical's open line of credit to Penphil that this and other conflict-of-interest situations could and did exist.

The dual roles played by Bevan and Hodge—controlling Penn Central investments in a way designed to benefit Penphil, which they also controlled—involved the manipulative use of Penn Central pension funds on which thousands of persons depend to sustain themselves in retirement. The question continually arises throughout Part III of the staff report: How could David Bevan simultaneously fulfill his fiduciary responsibility to Penn Central, to the beneficiaries of the pension funds under his control, and to the corporations in which the Penn Central had made heavy investments and whose boards were controlled by Bevan and Hodge by virtue of interlocking alliances and directorships? The question is repeatedly answered in a number of instances in this report; the details of the transactions disclose that Penphil stood to be the ultimate beneficiary.

The investigation of the Penn Central thus far has illustrated the undeniable need for legislation to accomplish the following:

1. Require examination by Federal bank supervisory agencies of loans and other financial transactions between individuals and commercial banks when these same lending institutions are providing loans and other financial services to commercial and industrial entities in which these individuals or members of their families serve as officers, directors or employees.

2. Require full disclosure of the makeup of pension fund assets, and the sale and purchase of pension fund assets, when such lending institutions act as administrators of such pension funds.

3. Prescribe limitations on the investment of pension fund assets in any single enterprise to help assure that such funds are prudently invested in all cases where Federally regulated lending institutions act as administrators of pension funds.

In addition, the Penphil case should be examined by law enforcement and regulatory agencies on both the Federal and state level to determine whether there have been violations of securities, transportation or other laws and regulations.

The views and conclusions found in this staff report do not necessarily express the views of the Committee or any of its individual members.

Wright Patman
M. C.

WRIGHT PATMAN, *Chairman.*

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PENPHIL: THE MISUSE OF CORPORATE POWER

SUMMARY AND CONCLUSIONS

> "The Penphil Corporation was a small, informal investment company set up by a number of us who were linked by friendship to invest for capital appreciation. It was a very small affair and run quite informally. I was a stockholder."
>
> —*David Bevan testifying before the Commerce Committee, U.S. Senate, August 6, 1970.*

> " * * * actually we are thinking in terms of having a large number of shares of Penphil outstanding and going, you might say, public ultimately with Penphil and turn it at the same time into an aggressive acquirer of other companies so that we can build it up into a very substantial conglomerate holding and operating company."
>
> —*David Bevan in a letter to Charles Hodge dated July 31, 1967.*

Despite public statements to the contrary, it is clear from a careful examination of the operations of the Penphil Company that it was intended to be, and was in fact, far more than an investment club.

Penphil, originally established in 1962 by David Bevan and Charles Hodge along with fourteen business associates and friends, was intended to be the principal vehicle by which control of important corporations was to be gained through various devices. In order to carry out this plan, it was necessary to acquire a substantial line of credit for Penphil. This was acquired by David Bevan and Charles Hodge from the Chemical Bank of New York City on an unusually favorable basis beginning in August 1962. This major lending institution, having provided more than $1.8 million in loans to Penphil over a period of seven years, played an essential role in making the overall plan work. Without this line of credit, it is doubtful that the members of Penphil would have been willing to put up the liquid assets necessary to carry out the plan. The $1.8 in Chemical Bank loans was the primary factor that has allowed Penphil investors to realize a 600 percent profit on their initial investment of $16,500 each in less than 8 years.

Another very important aspect of the Chemical Bank loan to Penphil should be highlighted. It was, to say the least, a highly concessionary loan agreement: (1) there were no formal loan procedures or payment schedules; (2) the line of credit was at the prime rate, although usually such loans would have been at a minimum of one percentage point above prime; (3) there was no compensating balance asked or required for these loans, although a 20-percent compensating balance would have been normal for a loan from a big New York bank.

It is clear, therefore, that the $1.8 million in loans to Penphil were not made by Chemical Bank on the basis of the soundness of the line of credit. They were made on preferential terms, as compared to loans of a similar nature, because of the value to Chemical Bank of Penn Central's loan and deposit business. In effect, it was Penn Central's compensating balances, interest payments and deposits that were subsidizing the Penphil line of credit for the personal profit of Penphil members.

It is also clear from an examination of the facts that Penphil was run almost exclusively by two men—David Bevan and Charles Hodge—despite the fact that its membership varied from 16 to 26 persons from its founding to the present time. Bevan and Hodge between them had access not only to bank credit but also to large sums of investable assets through such entities as the Penn Central Supplemental Pension Plan, with assets of more than $300 million, and the Penn Central Contingent Compensation Fund, with assets of over $11 million, along with the substantial assets of Glore Forgan, a major investment banking concern in which Hodge was a partner.

Thus, to a large extent, other peoples' money was being used to finance investments in certain selected companies for the purpose of permitting Penphil and those associated with it to control these same companies. Such activity raises extremely serious questions, especially when considering the fiduciary responsibility involved in managing the investments of a pension fund, on which thousands of actual and potential pensioners are relying for their income in retirement.

In addition to the questionable use of other people's money for the benefit of personal financial gain and personal interests, a number of the situations discussed in this report raise serious issues concerning the use of insider information to benefit the members of Penphil. This includes the purchase by Penphil of Great Southwest Corporation stock and its subsequent sale seventeen months after Penn Central gained control of Great Southwest. On this sale, Penphil realized a net profit of $212,500, a 130 percent return on its investment in less than 2½ years.

Another case in point is the investment by Penn Central through the supplemental pension plan in the stock of Tropical Gas, a company in which Penphil members held five of the ten director seats. The purchase of a large number of shares of Tropical Gas stock during a twenty-five day period in September and October of 1968 was a highly disadvantageous investment to the Penn Central Supplemental Pension Plan because Tropical Gas had already planned to make a new offering of stock on October 15, 1968, 25 days after the pension fund began increasing its investment in Tropical stock by more than

SOURCES OF FUNDS, INTERLOCKS AND PENPHIL INVESTMENTS

SOURCES OF FUNDS

CHEMICAL BANK NEW YORK TRUST COMPANY

Provided loans to Penphil for investment purposes.

PENPHIL COMPANY

Private investment club consisting of 26 individuals

INVESTMENTS

—Great Southwest Corp.
—Kaneb Pipe Line Co.
—Tropical Gas Co., Inc.
—Continental Mortgage Investors
—National Homes Corp.
—University National Bank of Boca Raton, Florida
—First Bank and Trust Co. of Boca Raton (N.A.), Florida
—Holiday International Tours

PENN CENTRAL TRANSPORTATION CO.

Sources of Funds Used for Investment Purposes

—Contingent Compensation Fund
—Employees Supplemental Pension Plan
—Pennsylvania Company
—Buckeye Pipe Line Company (Employees Benefit Funds)

GLORE FORGAN

—Company's own investments
—Personal investments of officers

Other Tie-Ins

—Investment advisor to Penn Central
—Investment banker for Kaneb, Tropical, and Great Southwest

INDIVIDUALS CONTROLLING INVESTMENTS

DAVID BEVAN

—Founded Penphil and controlled its investment program.
—Chief Financial Officer of Penn Central—Controlled all of Penn Central's investments, including those made by the Supplemental Pension Plan and the Contingent Compensation Fund.
—Director of:
Kaneb Pipe Line Co.
Great Southwest Corporation.
Tropical Gas Co., Inc.
Arvida Corporation.

CHARLES HODGE

—Major principal in the establishment of Penphil and the control of its investment program.
—Principal officer of Glore Forgan.
—Financial advisor to Penn Central.
—Officer and director of Great Southwest Corp.
—Director of:
Tropical Gas Co., Inc.
Executive Jet Aviation.
Arvida Corporation.

COMPANIES INVESTED IN

KANEB PIPE LINE CO.

—Two interlocks with Penphil.
—One interlock with Penn Central.
—One interlock with Tropical.
—Glore Forgan served as investment banker.

GREAT SOUTHWEST CORP.

—Four interlocks with Penphil.
—Four interlocks with Penn Central.
—One interlock with Glore Forgan.
—Glore Forgan served as investment banker.

TROPICAL GAS CO., INC.

—Six interlocks with Penphil.
—One interlock with Penn Central.
—Three interlocks with Glore Forgan.
—Glore Forgan served as investment banker.

UNIVERSITY NATIONAL BANK OF BOCA RATON, FLORIDA and FIRST BANK AND TRUST CO. OF BOCA RATON (N.A.), FLORIDA

—Each bank had two interlocks with Penphil.

ARVIDA CORPORATION

—Controlled by Penn Central
—Considerable real estate development activity in Boca Raton, Florida
—Six interlocks with Penphil
—Four interlocks with Penn Central
—One interlock with Glore Forgan

HOLIDAY INTERNATIONAL TOURS

—Company established and controlled by Penphil.
—Primary purpose to serve as general sales agent for International Air Bahama.

EXECUTIVE JET AVIATION

—Controlled by Penn Central.
—Controlled International Air Bahama.
—Three interlocks with Penphil.

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$1 million. This new issue would have inevitably diluted the value of the outstanding Tropical stock after the pension fund purchase was made. Bevan and Hodge, members of Tropical's Executive Committee, knew of the plans for the new issue before the pension fund started buying Tropical stock in September 1968 but did nothing to prevent this harmful action from taking place.

These purchases of Tropical stock also occurred immediately prior to an attempted takeover of Tropical Gas by another corporation, Mapco, thus raising the question of whether Bevan and Hodge were using the Penn Central pension fund (1) to protect Tropical Gas from a takeover rather than managing the pension fund strictly as an investment for the best interests of the beneficiaries of that fund, and (2) help maintain Penphil's ability to control Tropical.

Another questionable activity carried out by Penphil in connection with investments of the Penn Central Company was Penphil's purchase of large blocks of stock in two banks in Boca Raton, Florida, at a time when the Penn Central subsidiary, Arvida, was carrying out an intensive program of real estate development in the Boca Raton area. Was this Penn Central investment in Arvida pursued at least partly to enhance the value of Penphil investments in the same area? As a result of the dramatic growth in the Boca Raton area, partly based on Arvida's development program, the value of Penphil's bank investment grew by over $800,000, or more than 191 percent in a little over three years.

The view has been widely held that Penn Central's investment decisions in the last few years made in connection with its diversification program seemed simply to have reflected bad judgment by management. However, a detailed examination of the facts presented in this report indicates that these decisions make a great deal more sense when viewed in the light of the interests and goals of Penphil and its members. Some of these questionable investments are highlighted in the schematic chart facing page 2, indicating the principal relationships described in the body of this report.

A number of broader questions are raised by the activities of Penphil as described in the body of this report. Among these are:

(1) The propriety of commercial banks making substantial preferential loans to individuals for their personal use and profit on the basis of their positions as influential officers or directors of the bank's major corporate customers.

(2) The inherent conflict of interest involved in the same person carrying out at the same time such potentially conflicting roles as chief financial officer of a major corporation, a principal in the investment management of millions of dollars of trust funds held for the benefit of others; a principal in the investment of funds for a private investment company designed to develop into a significant holding and operating company; and an active director in companies over which control by the budding holding-investment company is sought.

(3) The question of making personal profits on the basis of insider information obtained while trying to carry out one's fiduciary responsibility as a corporate officer and/or director.

(4) The propriety of one individual acting as an investment advisor, investment banker and broker for a number of corporations and others entitled to sound and, above all, objective investment advice, at the same time becoming personally involved in the management and control of corporations through large equity interests, directorships and other close relationships.

Classic examples of such problems described above can be found in the roles played by David Bevan and Charles Hodge in connection with the operation of Penphil.

David Bevan was (1) The Chief Financial Officer of the Penn Central Company; (2) the Chairman of the management committee for the Penn Central Supplemental Pension Plan and the administrator of the Penn Central Contingent Compensation Fund; (3) a founder of, a stockholder in and a chief investment advisor to Penphil; (4) on the Board of Tropical Gas; (5) on the Board of Great Southwest Corporation; (6) on the Board of Kaneb Pipe Line Company; and (7) on the Board of Arvida Corporation.

To whom did David Bevan owe his greatest fiduciary responsibility? A fiduciary responsibility is not supposed to be divisible, i.e. one who has a fiduciary responsibility is not supposed to put himself in a position of divided loyalty. It would seem to be impossible for one in the position that David Bevan was in to faithfully carry out his duty to all the parties to whom he owed a fiduciary responsibility. Similar questions can be raised for other persons involved with the Penphil-Penn Central-Glore Forgan complex.

Similarly, Charles Hodge and/or his investment banking firm were (1) the principal investment advisor to Penn Central; (2) investment advisor to and broker for the Penn Central Supplemental Pension Plan and the Contingent Compensation Fund; (3) investment banker for Kaneb Pipe Line, Tropical Gas and Great Southwest Corp.; (4) a director of Great Southwest Corp., Arvida Corp. and Tropical Gas; and (5) holders of substantial investments in Kaneb Pipe Line, Tropical Gas and Great Southwest. How could Charles Hodge give sound objective investment advice to clients of Glore Forgan concerning their investments while being so personally involved in the management and control of these significant corporations?

Extremely serious questions of public policy are raised by the story told in detail in the body of this report. Serious consideration should be given to enacting legislation adequately safeguarding the public, users of bank credit, clients of investment bankers and advisers, stockholders, and beneficiaries of pension funds and other trusts, from the serious abuses that appear to have occurred as a result of the kind of conflict of interest and insider trading activity that resulted from the operation of Penphil.

ESTABLISHMENT OF PENPHIL

Penphil was incorporated in Pennsylvania on July 10, 1962, as an investment company. Initially, there were sixteen investors. Subsequent additions, less deletions, have raised the total number of investors to 26.

A list of Penphil investors along with their principal business positions, the number of shares owned in Penphil and the date on which they were acquired is shown on pages 6 to 8.

Name	Position	Number of shares	Date acquired
David C. Bevan	Formerly—Chairman of the Finance Committee and Member of Board of Directors, Penn Central Chairman, Manager of Pensions of Penn Central Director of Pennsylvania Company, Arvida, Great Southwest, and various other subsidiaries of Penn Central Director of Tropical Gas Co., Inc., and Kaneb Pipe Line Co.	3, 300	Sept. 7, 1962
Thomas R. Bevan	Brother of David Bevan Partner in law firm of Duane, Morris & Heckscher	3, 300	Sept. 7, 1962
Warren H. Bodman	Partner, Yarnall, Biddle & Co	3, 300	Sept. 7, 1962
Francis A. Cannon	Administrative V. P., First Boston Corp	3, 300	Sept. 7, 1962
Paul D. Fox (Retired)	Vice President, Administration, Penn Central	3, 100	Sept. 7, 1962
William R. Gerstnecker	Vice Chairman, Provident National Bank [1] Former V.P.-Corporate, Penn Central; Formerly Director, Arvida, Great Southwest	3, 300	Sept. 7, 1962
Robert Haslett	Vice President, Investments, Penn Central	3, 300	Sept. 7, 1962
Mrs. Marie L. Hodge	Wife of Charles J. Hodge of F. I. duPont-Glore Forgan & Co.,—a Director of Arvida, Great Southwest and Tropical Gas Former Director of Executive Jet Aviation	3, 300	Sept. 7, 1962
Frederick B. Holmes	V.P., Gladfelter Paper Company	3, 300	Sept. 7, 1962
Benjamin F. Sawin	Chairman of the Board, Provident International Corp	3, 300	Sept. 7, 1962
Mrs. Dorothy B. Stevens	Wife of Lawrence M. Stevens, deceased former partner, Hornblower & Weeks-Hemphill, Noyes	3, 300	Sept. 7, 1962
Mrs. Dorothy H. Warner	Wife of Theodore K. Warner, former V.P.—Accounting and Taxation, Penn Central	3, 300	Sept. 7, 1962

Angus G. Wynne, Jr	President and Chief Executive Officer, Great Southwest; Director, Arvida	3, 300	Sept. 21, 1962
Fred H. Billups (recently deceased).	Formerly—President, Tropical Gas; Director of Executive Jet Aviation	3, 000	July 1, 1963
Herbert E. Fisher	Chairman of the Board, Kaneb Pipe Line Co.; President & Chairman of the Board, Pipe Line Technologists, Inc.	3, 300	July 1, 1963
Edwin B. Horner	First Colony Life Insurance Co	3, 300	July 1, 1963
Hobart C. Ramsey	V.P., Glore Forgan	3, 300	July 1, 1963
Samuel A. Breene	Attorney, Oil City, Pennsylvania	3, 300	June 1, 1967
Joseph W. Davin	First V.P., Stockton, Whatley, Davin & Co V.P. and Director, Arvida.	577	Feb. 19, 1968
O. F. Lassiter	Formerly—President, Executive Jet Aviation	408	Feb. 19, 1968
Alfonso Manero	Retired partner of Glore Forgan	407	Feb. 19, 1968
Harry F. Ortlip	President, Harry T. Ortlip Co. (Box Hill Realty)	1, 323	Feb. 19, 1968
Brown L. Whatley	President, Arvida; Chairman of Board, Stockton, Whatley, Davin & Co.	1, 323	Feb. 19, 1968
Cornelius A. Dorsey	Assistant to Robert Haslett, Penn Central	715	August 1968
Thomas F. Fleming, Jr	Chairman of Board, First Bancshares of Florida, Inc	2, 285	August 1968
Vincent G. Kling	Architect	3, 300	Feb. 26, 1969

[1] William R. Gerstnecker announced his resignation as Vice Chairman of the Provident National Bank on January 19, 1971.

In addition to the above, the four individuals listed below were members of Penphil at one time:

Name	Position	Period during which a Penphil stockholder
Edward D. Meanor (Deceased)	Investments	Sept. 7, 1962–Dec. 1966
John K. Acuff (Deceased)	Brooke, Sheridan, Bogan & Co., Inc.	Sept. 7, 1962–Dec. 1964
C. Carroll Seward	Yarnall, Biddle & Co	Sept. 7, 1962–Jan. 6, 1969
Leslie M. Cassidy (Deceased)	Former Chairman of Johns-Manville Corp.	Sept. 7, 1962–Feb. 7, 1967

There are one million shares of Penphil common stock authorized, with a par value of $2.00 per share. At present, there are about 69,000 shares issued and outstanding.

PENPHIL INVESTMENT PROGRAM

Primarily with funds obtained through loans from Chemical Bank in New York, Penphil made eight major stock investments between 1962 and 1969, as detailed below.

Name of company	Number of shares acquired	Date acquired	Price paid
Kaneb Pipe Line Co	[1] 30,488	July 25, 1962 to Apr. 7, 1963	$153,247
Tropical Gas Co., Inc.[2]	10,000	Aug. 6, 1963 to Sept. 5, 1963	191,495
Continental Mortgage Investors	[3] 30,000	May 26, 1964	196,800
Great Southwest Corp	10,000	July 18, 1963	165,000
First Bank & Trust Co. of Boca Raton [4]	21,380	Oct. 13, 1966 to Sept. 10, 1968	332,924
University National Bank of Boca Raton [4]	4,868	Jan. 24, 1967 to Apr. 7, 1967	94,184
National Homes Corp	5,000	June 5, 1968 to June 6, 1968	74,370
Holiday International Tours	51,000	Feb. 21, 1968	25,000

[1] Penphil also holds warrants to purchase 7,653 additional shares of Kaneb common stock.

[2] Exchanged for 8,900 shares of U.S. Freight Co. as result of merger with Tropical in October 1969.

[3] Now 60,000 shares as a result of a 2-for-1 stock split in January 1970.

[4] Merged with 2 other Florida banks into First Bancshares of Florida, Inc., a registered bank holding company, in 1970.

CHEMICAL BANK SUPPLIES THE FUNDS

A description of how Penphil and Chemical Bank got together and how Penphil used the power of the Pennsylvania Railroad (subsequently the Penn Central Transportation Co.) to promote favorable loan conditions for itself is contained in a Chemical interoffice memorandum written in 1962 by C. A. McLeod, now Vice President of Chemical's International Division, and distributed to W. S. Renchard, now Chairman of Chemical's Board of Directors, and M. A. Chamberlain, Vice President of the bank's Metropolitan Division. The memorandum states in part:

> David Bevan, financial vice president of the Pennsylvania Railroad Company, called me on the telephone today and said that he and a group of friends, totaling about fifteen, are planning to organize a corporation to purchase a substantial block of common stock of Kaneb Pipe Line Company [Penphil's first investment]. The group will include Charlie Hodge of Glore Forgan and Company, Benjamin F. Sawin, president of Provident Tradesmen's Bank and Trust Company [now Provident National Bank], Messrs. Gerstnecker and Haslett of the Pennsylvania Railroad's financial staff and others.
>
> Frankly the rate [prime rate] on the proposed loan is too low, but, in view of the size of the deal and the fact that it has such good friends connected with it, WSR [W. S. Renchard, Chairman of Chemical's Board of Directors] felt it was preferable not to quibble with Mr. Bevan over the rate. He indicated that George Bartlett of Glore Forgan and Company would probably be the one to negotiate the purchase of the stock and very likely Charlie Hodge would be the one to work out the mechanics of the loan arrangement.

In effect, the mechanics that were worked out on the loans, which totaled more than $1.8 million, consisted of establishing an open-ended line of credit without any prescribed requirements regarding the payment of interest or principal. Until last June, all loans made to Penphil under this line of credit were at the prime rate—the lowest interest rate available to the largest and most secure borrowers of the bank. Stock purchased with the Penphil loans was used as collateral to secure the loans themselves. Chamberlain, who supervised the Penphil account for Chemical, has stated that the rate went to one point above the prime rate in June 1970 because money was very tight at that time.

The following table shows Penphil's loans from Chemical Bank and stock purchases:

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TABLE 1.—*Penphil loans from Chemical Bank* [1] *and stock purchases*

Schedule of Penphil loans from Chemical Bank [2]		Schedule of Penphil stock purchases			
Date of loan	Amount of loan	Date of purchase	Name of stock	Number of shares	Cost of investment
Aug. 20, 1962	$102,000.00	July 25, 1962	Kaneb Pipeline Co	19,000	$95,082.35
Feb. 8, 1963	40,000.00	July 26, 1962	do	3,000	15,000.00
July 25, 1963	115,000.00	July 27, 1962	do	633	3,165.00
Aug. 6, 1963	5,000.00	Feb. 7, 1963	do	5,000	40,000.00
Aug. 8, 1963	47,450.00	July 18, 1963	Great Southwest Corp	10,000	165,000.00
Aug. 14, 1963	25,012.30	Aug. 1, 1963	Tropical Gas Co	4,100	74,637.50
Aug. 16, 1963	27,187.50	Aug. 7, 1963	do	1,315	25,012.30
Aug. 26, 1963	30,026.25	Aug. 14, 1963	do	200	3,950.00
September 1963	45,636.75	Aug. 19, 1963	do	1,700	34,011.25
Sept. 11, 1963	8,057.52	Aug. 23, 1963	do	400	8,057.52
Sept. 13, 1963	4,000.00	Aug. 28, 1963	do	2,000	40,075.00
Sept. 20, 1963	3,749.95	Aug. 29, 1963	do	285	5,751.70
Mar. 24, 1964	1,739.65	May 26, 1964	Continental Mortgage Investors	10,000	196,800.00
May 25, 1964	196,800.00	Sept. 27, 1966–Jan. 12, 1967.	First Bank & Trust Co. of Boca Raton.	8,112	242,174.50
Dec. 29, 1965	379,000.00				
Sept. 15, 1966	15,000.00	Jan. 24, 1967–March 1967.	University National Bank of Boca Raton.	2,928	62,640.00
June 29, 1967	10,000.00				
Oct. 17, 1967	40,000.00	Apr. 7, 1967	do	1,700	31,544.50
Nov. 2, 1967	492,000.00	Feb. 21, 1968	Holiday International Tours	51,000	25,000.00
Nov. 3, 1967	1,000.00	June 5, 1968	National Homes Corp	200	2,937.50

See footnotes at end of table, p. 12.

TABLE 1.—*Penphil loans from Chemical Bank* [1] *and stock purchases*—Continued

Schedule of Penphil loans from Chemical Bank [2]		Schedule of Penphil stock purchases			
Date of loan	Amount of loan	Date of purchase	Name of stock	Number of shares	Cost of investment
Jan. 22, 1968	$41, 549. 16	June 6, 1968	National Homes Corp	4, 800	$71, 433. 03
June 24, 1968	50, 000. 00	June 27, 1968	Loan to Holiday by Penphil		40, 000. 00
June 25, 1968	40, 000. 00	Sept. 10, 1968	First Bank & Trust Co. of Boca Raton.	1, 815	90, 750. 00
Aug. 30, 1968	60, 000. 00				
Oct. 4, 1968	30, 000. 00				
Total	1, 810, 209. 08		Total		[3] 1, 273, 022. 15

[1] All loans were made by the Chemical Bank New York Trust Co. at the prime rate.
[2] Data on loans obtained from Chemical Bank New York Trust Co.
[3] Total does not include Penphil's investments in short-term paper, Government securities, or long-term debentures.

When questioned by staff investigators, Chamberlain said that under normal conditions Chemical would make such loans at an interest rate that was at least one point above the prime and that a "decent" compensating balance would be required from Penphil. By "decent" Chamberlain said he meant that an amount equivalent to about 20 percent of the outstanding balance of the loans would have to have remained on deposit in a Penphil account in the bank. Penphil did maintain a checking account at Chemical, but the amount on deposit fluctuated markedly, and the average amount—about $4,000—was far from 20 percent of the $500,000 to $800,000 outstanding balance that was usual on the Penphil loans. In fact, it was less than one percent.

Chamberlain said that normal loan requirements were not applied to the Penphil loans because of "other considerations which compensated the bank". These other considerations, according to Mr. Chamberlain, consisted of the following:

1. One of the bank's major accounts consisted of loan transactions with the Penn Central—an arrangement which, among other things, required maintenance of a compensating balance.

2. David Bevan was known to senior officers of Chemical. He was so well known, in fact, that he has had a line of credit for personal loans with the bank predating the formation of Penphil. The unpaid balance on this account, bank sources said, reached a high point in 1967 when Bevan owed Chemical about $150,000. For the most part, the loans were used for private stock investments. However, in one instance, Chemical loaned Bevan $55,000 on an unsecured basis after Bevan had produced satisfactory evidence that he was worth $1 million. The money was used to purchase a condominium apartment in Boca Raton, Florida, from the Arvida Corporation, which is now controlled by Penn Central. All of Bevan's personal loans from Chemical were at the prime rate, a situation enjoyed by few individuals in the nation, no matter how wealthy or powerful they are. In December 1970, the outstanding balance on Bevan's loans at Chemical was $16,000.

3. Chamberlain had a longstanding professional relationship with Charles Hodge based on bank transactions with Glore Forgan (now F. I. duPont, Glore Forgan) and private loans made to Hodge and his wife for stock investments and other purposes. The unpaid balances of Chemical Bank's loans to Hodge and his wife totaled almost $950,000 in November 1968.

Chamberlain said that $350,000 to $400,000 was loaned to Hodge in 1970 so that he in turn could use these funds to shore up the crumbling financial structure of Glore Forgan. Glore Forgan senior debentures were assigned to secure this loan—which means that if Glore Forgan had collapsed, Chemical security for this loan would have been worthless. (Chamberlain said that Chemical made 15 or 20 loans in 1970 to other investment banking firms which had similar financial problems).

4. Professional business relationships also existed between Chemical and other Penphil stockholders involved in the investment banking field.

5. Chamberlain said that all the Penphil stockholders with whom he was acquainted were "responsible people".

6. The Penphil loans, Chamberlain said, were "fully and properly secured". Chamberlain said that by this he meant that stock purchased with the loans to Penphil together with the income from these securities was pledged to secure the loans.

Penphil's first investment consisted of the purchase of 22,633 shares of Kaneb Pipe Line at a cost of $113,247, in July of 1962. Ninety percent of the total cost, $102,000, was provided by Chemical in its first loan to Penphil. This type of transaction, with Chemical providing a maximum amount of money and Penphil providing a minimum amount, typified transactions between the two throughout the history of Penphil. The unpaid balance of the Penphil account reached its highest point in June of 1968 when it totaled $1.2 million. That year also marked the highest point reached in terms of the market value of Penphil investments, $3.2 million.

As indicated above, the Penphil-Chemical relationship was established with remarkable ease, and from that time on the transactions between the two were conducted without hesitation.

Generally, small blocks of Penphil stock, ranging from 100 to 300 shares, were sold to each of the existing stockholders twice a year, in January and June. The proceeds would be applied against the accrued interest on the Chemical loan, and the remainder was used to reduce the principal. All dividends earned by the Penphil investments, and the proceeds from the sale of stock held by Penphil in Great Southwest, U.S. Freight Co. and National Homes were applied against the unpaid balance of the loans which in December of 1970 had been reduced to $280,000.

Chamberlain said that from time to time he would meet with Hodge, who would give Chamberlain instructions about receiving and delivering stock in connection with Penphil investments. These instructions would later be confirmed in writing from Thomas Bevan in Philadelphia.

In this way, most of the Penphil shareholders were required to invest only $16,500 of their own money as of December 1970. The balance of the investment funds came from Chemical Bank loans, dividends and capital gains from the sale of securities. As a result of this arrangement and the appreciated value of Penphil investments, the original Penphil shareholders each hold stock having a net value of about $100,000—or a 600 percent return on their cash investment. Each share of Penphil stock was valued at $35 in December 1970.

When questioned by staff investigators, Chamberlain said he was not aware that Penphil held common investments with the Penn Central in Tropical Gas, Kaneb Pipe Line, Continental Mortgage and National Homes until press reports revealing this were published during the summer of 1970. On further questioning, Chamberlain said he was aware that Penphil sold its stock in the Great Southwest Corporation in order to avoid a conflict of interest situation after control of that company had been purchased by Penn Central. (This transaction is detailed elsewhere in this report.) When asked whether the sale of Great Southwest stock by Penphil had prompted him to examine other Penphil investments to determine the possible existence of other conflict of interest situations, Chamberlain replied it had not. Indeed, Chamberlain said he would not have been concerned about the

Penphil situation even if he had known from the beginning that Penphil held common investments with Penn Central in the four companies noted above, "as long as all the cards were on the table."

Chamberlain said that Thomas Bevan, in August of 1970, asked him how much interest had accrued at that time on the unpaid balance in the Penphil account and indicated that Penphil stockholders intended to liquidate the corporation. Nothing was heard from Thomas Bevan during the ensuing two weeks, and at the end of that time Chamberlain called Bevan to ask if there were instructions that he should be following regarding the liquidation of Penphil assets. He said that Bevan told him then that Penphil stockholders were not going to sell out after all. Nevertheless, Chamberlain said he understood that Penphil shareholders intended to liquidate in the foreseeable future.

His statements regarding Penphil were given to staff investigators on December 21, 1970. At that time, Chamberlain said he was not aware of a December 9, 1970, Penphil stockholders' meeting in Philadelphia, when it was decided by an overwhelming vote to rescind a previous decision to liquidate and to continue the corporation for an indefinite time. Chamberlain indicated that under these circumstances Chemical's loan arrangements with Penphil might have to be re-examined from the point of view of imposing additional requirements, such as a compensating balance. By the same token, he also indicated that continuation of the Penphil account under existing, dormant conditions, stemming from the fact that Penphil has made relatively few investments during its entire history and none recently, would be less than satisfactory to Chemical. "We can't let this thing drag on forever this way," he asserted.

The reason for Chemical's changed attitude toward Penphil is obvious. The Penn Central Transportation Co. had collapsed and so had its ability to maintain a large compensating balance and to retire the outstanding balance on its loans from Chemical. Therefore, the overriding incentive to Chemical to carry the Penphil account under what can only be regarded as privileged circumstances no longer existed.

COMMON INVESTMENTS OF PENPHIL AND PENN CENTRAL

With the exception of the investments in the two Florida banks and Holiday International Tours (HIT), all of the major investments of Penphil have one important factor in common—Penn Central also invested in the stock of these five companies at approximately the same time as Penphil. Furthermore, Penphil's investments in the two Florida banks and HIT are directly related to Penn Central's investments in the Arvida Corporation and Executive Jet Aviation, Inc., as detailed in other sections of this report.

The establishment of Penphil and the control of its investment program can be primarily attributed to two men—David Bevan and Charles Hodge. The Penn Central investments in the subject companies were controlled by David Bevan. At the same time, Charles Hodge served as the investment advisor to Penn Central.

Table 2 which follows shows the common investments of Penphil and Penn Central.

TABLE 2.—*Common investments of Penphil and Penn Central*

Name of company	Penphil: Number of shares acquired	Penphil: Time period	Penn Central: Number of shares acquired	Penn Central: Time period
Kaneb Pipe Line Co	[1] 30, 488	July 25, 1962–Feb. 7, 1963	[2] 122, 500	Nov. 11, 1960–Dec. 3, 1968.
Tropical Gas Co., Inc	[3] 10, 000	Aug. 6, 1963–Sept. 5, 1963	[4] 89, 400	Feb. 26, 1960–Oct. 15, 1968.
Continental Mortgage Investors.	[5] 30, 000	May 26, 1964	[5] 112, 500	Apr. 6, 1962-Dec. 31, 1969.
Great Southwest Corp	[6] 10, 000	July 18, 1963	23, 902, 750	Jan. 29, 1963–December 1969.
National Homes Corp	[3] 5, 000	June 5, 1968–June 6, 1968	[7] 10, 000	Sept. 13–17, 1968.

[1] Penphil also holds warrants on 7,653 shares of Kaneb common stock.
[2] Penn Central also holds warrants on 41,021 shares of Kaneb common stock.
[3] Penphil's holdings in Tropical Gas (U.S. Freight Co.) and National Homes were sold in the summer of 1970.
[4] Exchanged for 79,566 shares of U.S. Freight Co., as result of merger in October 1969.
[5] Subsequently, on Jan. 15, 1970, there was a 2-for-1 stock split.
[6] Sold its shares on Dec. 7, 1965.
[7] Sold 8,700 of these shares between May 13 and Sept. 24, 1969.

An analysis of the Penn Central holdings in the five companies shown in table 2 indicates that, with the exception of its holdings in Great Southwest, the investments were made primarily through the Railroad's Contingent Compensation Fund and the Supplemental Pension Plan. Both of these funds were under the direct control of David Bevan.

The Contingent Compensation Fund consists of deferred compensation for officers of the Railroad and certain of its subsidiaries. The Fund's holdings, which had a market value of about $11.5 million at December 31, 1969, are considered to be assets of the Railroad.

The Supplemental Pension Plan represents pension rights belonging to about 21,700 active and 15,200 retired employees of the Railroad and 34 of its subsidiary companies. At December 31, 1969, the Plan's holding had a book value of over $278 million and the market value of the holdings totalled about $331 million. The funds in the plan are not considered to be assets of the Railroad.

Presented in the following table is a breakdown of the Railroad's holdings in the five companies under discussion:

TABLE 3.—*Penn Central stockholdings in 5 companies in which Penphil invested*

Name of company	Total Penn Central holdings	Pension plan holdings	Percentage of total holdings	Contingent compensation fund holdings	Percentage of total holdings	Other holdings	Percentage of total holdings
Kaneb Pipe Line Co	[1] 122, 500	80, 000	65	35, 500	29	[2] 7, 000	6
Tropical Gas Co., Inc	89, 400	87, 400	98	2, 000	2	---	---
Continental Mortgage Investors	112, 500	[3] 105, 750	94	([3])	---	[3] 6, 750	6
National Homes Corp	[4] 10, 000	---	---	9, 700	97	[2] 300	3
Great Southwest Corp	23, 902, 750	73, 900	---	81, 000	---	[5] 23, 747, 850	99

[1] In addition, Penn Central holds warrants on 41,021 additional shares of Kaneb common stock, as follows: Pension plan, 32,143; contingent compensation fund, 4,286; and Buckeye annuity plan, 4,592.

[2] These shares are held by the Buckeye Pipe Line Co.'s annuity plan fund and contingent compensation fund.

[3] Subsequently, on Jan. 15, 1970, there was a 2-for-1 stock split, raising the holdings of the pension plan to 211,500 and the "other holdings" to 13,500. In addition, on Feb. 24, 1970, the contingent compensation fund purchased 1,000 shares.

[4] Sold 8,700 of these shares between May 13, 1969 and Sept. 24, 1969.

[5] Shares held by the Pennsylvania Co., a wholly owned subsidiary of the Penn Central Transportation Co.

It can be seen from table 3 that with the exception of the investments in National Homes Corp. and Great Southwest Corp., the majority of the funds used in the Penn Central's common investments with Penphil came from the employees' Pension Plan.

Common Investments—Two Classifications

An analysis of the five common investments of Penphil and Penn Central shows that they can be classified into two separate groupings, as follows:

1. Kaneb Pipe Line Co.; Tropical Gas Co., Inc.; and Great Southwest Corp.
2. Continental Mortgage Investors; and National Homes Corp.

The former grouping represents those companies that were interlocked with the Penn Central-Penphil-Glore Forgan combine. For each of the three companies, the President or principal officer became a member of Penphil. One or more Penn Central and Penphil members became or were directors of the companies. The combined stockholdings of Penphil, its members, Glore Forgan, its members, and Penn Central in these companies made it possible for the Penphil-Penn Central-Glore Forgan combine to control each of these three companies. For all three of these companies, Glore Forgan served as the investment banker.

The second grouping represents a completely different picture. There were no interlocks between these companies and Penphil, Glore Forgan and Penn Central. The combined stockholdings in these companies by the Penphil-Penn Central-Glore Forgan combine were insufficient to allow the combine to have any significant control over these two companies. For both of these companies, Hornblower & Weeks-Hemphill, Noyes served as the investment banker.

Penphil's total investment in the five common companies amounted to $783,590. Of this amount, $512,420 was invested in the stocks of Kaneb, Tropical and Great Southwest. This amount represented over 65 percent of Penphil's total investment in these five companies. Penphil's investment in Continental Mortgage and National Homes totalled $271,170, or less than 35 percent of Penphil's total investment in the five companies.

The Committee staff was informed by Charles Hodge that he advised Penphil to invest in Kaneb, Tropical and Great Southwest. He further stated that Lawrence Stevens of Hornblower & Weeks-Hemphill, Noyes, made the recommendations to Penphil regarding the investments in Continental Mortgage Investors and National Homes Corporation.

Through stockholdings and interlocks, Kaneb, Tropical and Great Southwest were deeply intertwined with the Penphil-Penn Central-Glore Forgan complex—so deeply, in fact, that David Bevan and Charles Hodge could exercise control over their operations.

MYSTERY OF PENPHIL

During the course of the investigation of the Penn Central Transportation Company, it became apparent to the committee staff that many, if not most, of the shareholders of Penphil did not participate in its investment decisions. Indeed, many, if not most, of the shareholders were unaware of what investments Penphil had made until after the fact. According to their statements, they paid little or no attention to these investments.

A case in point is William Gerstnecker. Gerstnecker is one of the original 16 members of Penphil and was Treasurer and a Vice President of the Penn Central. During his discussion with staff investigators, he described himself as "David Bevan's assistant."

Gerstnecker said that the original members of Penphil, for the most part, were friends of David Bevan and comprised the membership of a fishing club, "The Silverfish", which used to take annual or semi-annual fishing trips. Gerstnecker said he never went with the group because he did not have the time to do so.

During the first half of 1962, Gerstnecker said, David Bevan told him an investment club was being formed and asked if he (Gerstnecker) would like to join.

Bevan told him some of the group's members were "good investment people" and that the club "would have good advice" in this respect. Gerstnecker said he joined without hesitation.

Gerstnecker told staff investigators that he "was never consulted prior to any of Penphil's investments, with the exception of Holiday International Tours."[1] He stated that he knew about HIT because he was at a meeting when this was discussed.

Other than the HIT investment, Gerstnecker disclaimed having participated in any other Penphil investment decisions. The former Penn Central Treasurer said he was unaware of (1) the loan arrangements Penphil had made with Chemical Bank, (2) the nature of the Penphil-Florida bank investments, (3) Penphil's ability to control certain of the companies it invested in, and (4) the reasons behind the August 1970 decision to liquidate Penphil and the December 1970 decision to continue Penphil.

However, Gerstnecker said he was aware of David Bevan's intention to turn Penphil into a substantial holding and operating company and the fact that Penphil held common investments with Penn Central. He said he was not concerned about the common holdings.

Robert Haslett, who also worked under David Bevan at the Penn Central as Vice President-Investments, said that Bevan informed him in 1962 that "a little investment club" was going to be formed "to put some money to work and try and make some money," and he accepted the invitation to join. Haslett said he looked on the periodic Penphil stock purchases required of Penphil members as a "payroll deduction" over the years and did not pay much attention either to the $16,500 he ultimately invested in the company or to the investments made by Penphil itself.

He told staff investigators that he saw nothing wrong in the fact that Penphil held common investments with the Penn Central even though he admitted the necessity of Penphil having to sell its shares of Great Southwest to eliminate a conflict-of-interest situation after the Penn Central purchased controlling interest in that company. The sale, he added, did not prompt him to examine other common investments of Penphil and the Penn Central from the point of view of determining whether other possible conflict-of-interest situations existed.

[1] Penphil's investment in HIT, which is summarized later in this report, was previously detailed in Part II of the staff report—*Case Study of a Penn Central Subsidiary: Executive Jet Aviation.*

Like other Penphil shareholders questioned by staff investigators, Haslett said he was unaware of Penphil's investments until after they were made and knew nothing of the details of the company's investments in HIT, the Florida banks or of the special features of Penphil's loan arrangements with the Chemical Bank. It is difficult to understand how he could make this profession of ignorance concerning the activities of Penphil in view of the fact that he was a former Director, Vice President and Chairman of the Investment Committee for Penphil.

The same lack of knowledge concerning the details of Penphil's investments was also expressed by Thomas Bevan, even though he has been a Penphil officer since the founding of the company. Thomas Bevan, however, admitted knowledge of his brother's intention to turn Penphil into a conglomerate.

Similar responses were given to questions about Penphil by Thomas Fleming, Brown Whatley and Herbert Fisher. As noted elsewhere in this report, Fleming stated he was anxious to join Penphil because he was impressed with what he considered to be the financial stature of David Bevan and Charles Hodge. Whatley stated he joined Penphil to cement his relationship with David Bevan, who was directing the Penn Central's investment program. Fisher said he was invited to join by Bevan and did so because it looked like an opportunity to make some money. He said he paid no attention to Penphil because it represented a relatively small investment for him and he had more important matters with which he was concerned.

Documents obtained by the staff and statements made by Penphil shareholders make it clear that all final decisions regarding Penphil's activities were made by David Bevan and Charles Hodge. In effect, the activities of Penphil remained a mystery to most of its membership, while control was exercised by these two men.

A part of the mystery of Penphil includes the handling of a transaction involving the sale of $750,000 worth of Kaneb Pipe Line Company debentures to the National Newark and Essex Bank of Newark, New Jersey, in September of 1968. The $750,000 total included a $500,000 Kaneb debenture note held by Penphil. Details of the transaction are contained in the following correspondence.

A letter dated September 5, 1968, from Thomas Bevan to Melville P. Chamberlain, Vice President of Chemical Bank, states:

> This is to confirm my telephone conversation in which I requested you to forward to Donald Herterich, Vice President of Manufacturers Hanover Trust Company, 40 Wall Street, New York City, the $500,000 Kaneb debenture which we pledged with you as security for the loan.
>
> We are selling the $500,000 Debenture to the National Newark and Essex Bank for which there will be a closing on September 10 at which time we will request Mr. Herterich to forward to you $500,000 in reduction of our loan. We would appreciate it if you will deposit in our account the additional amount of $16,423.62 representing interest on the Debenture which will be paid to us at the same time.
>
> Mr. Herterich would appreciate receiving the Kaneb Debenture as soon as possible so that he can combine it with another debenture which is being sold to the same bank at that time.

A letter dated September 6, 1968, from Robert W. Loder, then Assistant Vice President of the Penn Central Transportation Company, to John N. Page, Vice President and Senior Investment Officer of the National Newark & Essex Bank, reads as follows:

> Your bank has agreed to purchase from us on September 10, $750,000 principal amount of Kaneb Pipeline Company 6⅞% Subordinated Notes dated December 19, 1967. These Notes are being sold to you at par together with accrued interest at 6⅞% from March 18, 1968, to September 9, 1968, inclusive, amounting to $24,635.43.
>
> The Notes are presently in possession of the Manufacturers Hanover Trust Company, Transfer Agent, and are being reregistered in the name of George & Co. [nominee name used by the National Newark & Essex Bank] for delivery to you.
>
> Will you please arrange to bank wire the sum of $516,423.62 to the Chemical Bank New York Trust Company, (Attn Melville Chamberlain, Vice President), Church Street Post Office Station, for credit of the account of Penphil, account number 066–106–397. The sum of $258,211.81 should be bank wired to Girard Trust Bank, Broad and Chestnut Streets, Philadelphia, Pennsylvania, for account of Mutual Fire, Marine and Inland Insurance Company, account number 2–2–061–737.
>
> For your information, I am attaching a copy of the Note Agreement pertaining to the extension and renewal of the Note you are purchasing. Your cooperation is very much appreciated.

Neither of the debentures involved in the above transaction was owned by Penn Central. Yet the sale was handled by a Penn Central employee who was not a member of Penphil, and the letter from Loder to Page was written on official Penn Central stationery.

Loder, an assistant to Bevan at the time of the subject transaction, told staff investigators that he did not remember the letter. Moreover, he added that he knew nothing of the transaction or why he handled the sale of a debenture owned by Penphil. He did acknowledge, however, after the letter was read to him by staff investigators, that he did write the letter and that these were not Penn Central-owned debentures.

KANEB PIPE LINE COMPANY

Penphil began investing in Kaneb in 1962, and continued purchasing stock through February 1963. Penphil owns 30,488 shares of Kaneb common stock. Penphil also holds warrants to purchase an additional 7,653 shares of Kaneb common stock.

In the summer of 1963, Herbert E. Fisher, Chairman of the Board of Kaneb, became a stockholder in Penphil. Mr. Fisher owns 115,496 shares of Kaneb common stock. Mr. Fisher is also co-trustee of two trusts for the benefit of his daughter. The trusts collectively own 24,835 shares of Kaneb common stock.

Mr. Fisher's feelings about being invited to join Penphil are expressed in the following letter:

> SEPTEMBER 16, 1963.
>
> To our Associates in the Penphil Co.:
>
> First let me thank you for the opportunity of being associated with such a fine group as represented by Penphil. I am sorry that Mr. Benjamin F. Sawin was unable to be present as he is the only one we have not as yet met. We are, of course, personally acquainted with Fred Billups and Angus Wynne.
>
> As you will recall, at the New York meeting I promised to keep the Penphil stockholders currently apprised of the status of Kaneb. In order to bring you up to date I am transmitting attached the 1962 annual report and the semiannual report ending June 30, 1963. Also, for the information of our new associates we are enclosing a copy of our engineering firm's brochure which briefly outlines the services we perform. It

should be remembered that Kaneb Pipe Line is operated under a long-term management contract by Pipe Line Technologists, Inc. Exclusive of full-time operating personnel, Kaneb officers and directors receive no direct remuneration other than that covered by the management contract. The primary incentive to the officers and directors is their ownership in the company and nominal stock options.

Pipe Line Technologists is strictly a firm of professional engineers which is in no way directly or indirectly connected with a construction contractor, supplier, or manufacturer. The firm enjoys a worldwide reputation and is presently negotiating for management operating contracts which should have the effect of further reducing the staff charges to Kaneb.

We would welcome an opportunity to visit with any of the Penphil members whenever they are in Houston or the vicinity of Kaneb facilities. Please do not hesitate to advise if we can be of any assistance to you at any time.

We shall look forward to becoming better acquainted with each of you personally through Penphil and our other joint ventures.

Sincerely yours,

HERB FISHER.

The Railroad, under David Bevan's supervision, began purchasing Kaneb common stock in November 1960. By December 1968, the Railroad had acquired 122,500 shares of Kaneb common stock. In addition, the Railroad holds warrants on an additional 41,021 shares of Kaneb common stock.

In 1963, David Bevan became a director of Kaneb. Mr. Bevan is the beneficial owner of 3,044 shares of Kaneb common stock.

Although Glore Forgan had no Board members on Kaneb, it was directly tied in with the company. In addition to being the investment banker for Kaneb, Glore Forgan and its members, at March 10, 1965, held beneficially almost 107,000 shares of Kaneb common stock.

Kaneb also had a common director with Tropical Gas Co., Inc.—Mr. Ralph W. Halsey, Jr. A Director of Kaneb since 1958, he was also a Director of Tropical since 1958.

By 1969, the combined stockholdings of Penphil, its members, and Penn Central amounted to almost 22 percent of the total outstanding common stock of Kaneb. (This total does not include any holdings by Glore Forgan, its members, or the trust holdings of Mr. Fisher's daughter.) The 22 percent stockholding in Kaneb was broken down as shown in the following table:

TABLE 4.—*Penphil group stockholdings in Kaneb Pipe Line Co.*

Total Kaneb common shares outstanding	Holdings of Penphil, its members, and Penn Central	Percent holdings of Penphil, its members, and Penn Central	Breakdown of Penphil, its members, and Penn Central holdings				
			Penn Central	Penphil	Herbert Fisher	David Bevan	Total holdings
1,259,053	[1 2 3 4] 271, 528	21. 56	[3] 122, 500	[3] 30, 488	[4] 115, 496	3, 044	271, 528

[1] Does not include any stockholdings of Glore Forgan or its members. Glore Forgan and its members held almost 107,000 shares at Mar. 10, 1965. Comparable information was not available for 1969.

[2] Does not include warrants held by the Penn Central for an additional 41,021 shares of Kaneb common stock.

[3] Does not include warrants held by Penphil for an additional 7,653 shares of Kaneb common stock.

[4] In addition, Mr. Fisher is the co-trustee of 2 trusts for the benefit of his daughter. The trusts collectively own 24,835 shares of Kaneb common stock.

The combined stockholdings of just Penphil, Penn Central and David Bevan, exclusive of the warrants held by Penphil and Penn Central, amounted to over 12 percent in 1969, as follows:

Total Kaneb common shares outstanding	Shares held by Penphil, Penn Central and Dave Bevan	Percent of total outstanding
1,259,053	156,032	12.39

The above facts demonstrate quite vividly that David Bevan was attempting to maneuver himself and Penphil into the same control position over Kaneb that was achieved in the cases of Tropical Gas, Great Southwest, Holiday International Tours, and the two Florida banks, as described in other sections of this report.

CONTINENTAL MORTGAGE INVESTORS AND NATIONAL HOMES CORPORATION

The Penphil and Penn Central investments in Continental Mortgage Investors and National Homes Corporation—the two common investments for which Glore Forgan was not the investment banker—present a completely different picture from the Kaneb, Tropical and Great Southwest investments.

No principal officer or director of Continental Mortgage or National Homes became a member of Penphil. No Penphil member went on the Board of Continental Mortgage or National Homes. No member of Glore Forgan served on the Boards of these two companies.

At no time did the combined stockholdings of Penphil and Penn Central rise above 2.14 percent of the outstanding common stock of either one of these two companies. The following table shows the holdings of Penphil and Penn Central as compared to the outstanding shares of these two companies.

Table 5.—*Penphil group stockholdings in noninterlocked companies*

Company	Total shares outstanding	Total Penphil and Penn Central holdings	Percentage of total shares outstanding	Breakdown of holdings	
				Penphil	Penn Central
Continental Mortgage Investors	6, 631, 932	[1] 142, 500	2. 14	[1] 30, 000	[1] 112, 500
National Homes Corp	4, 697, 264	15, 000	. 31	[2] 5, 000	[3] 10, 000

[1] Subsequently, on Jan. 15, 1970, there was a 2-for-1 stock split.
[2] Penphil disposed of this investment in the summer of 1970.
[3] Sold 8,700 of these shares between May 13, 1969, and Sept. 24, 1969.

The attitude of the Penphil hierarchy towards these two investments is best summed up in a letter from Charles Hodge to David Bevan concerning the National Homes investment, presented below:

Dear Dave: With reference to your letter of June 5, 1968 and memorandum from Ben [Sawin], I concur completely with Ben's recommendation and you have herewith my affirmative vote.

I was notified after the fact this morning that Penphil has bought 5,000 shares of National Homes. Larry [Stevens] called me and explained it was an oversight that I was not notified, and this oversight is understandable and I am certainly not put out. However, I must go on record, while this will be a popular and fast moving stock, I do not agree with the fundamental purpose nor do I agree with the management of the Price brothers who have not demonstrated any ability in this field. I am confident that stockmarketwise we will probably make some money in it, but would like to go on record that this is not one to hold blindly.

See you soon.

Sincerely,

CHARLES J. HODGE,
Chairman of Executive Committee.

PENPHIL INVESTMENT IN GREAT SOUTHWEST CORPORATION

Penphil's involvement with the Great Southwest Corporation (GSC) differs from the other common investments of Penphil and Penn Central in that Penn Central eventually acquired direct control of GSC. This control was established during the time period that Penphil held its investment in GSC.

A description of GSC and the nature of Penphil's and Penn Central's involvement with GSC follows.

Great Southwest Corporation

Great Southwest Corporation was incorporated in Texas on October 2, 1959, as the successor to two Delaware corporations incorporated in 1956. Since launching its initial enterprise, a 2,400-acre industrial park in Texas in 1956, GSC has become one of the nation's largest land developers.

In 1969, the California-based Macco Corporation—a 100%-owned subsidiary of the Penn Central Company—was merged into GSC. In addition to its real estate activities in Texas and California, GSC constructed and now operates, as the general partner in two limited partnerships, large amusement parks in Texas and Georgia. A third amusement park in St. Louis is currently under construction.

In recent years, GSC has entered the mobile home sales and manufacturing field by acquiring the nation's second largest independent manufacturer of mobile homes. GSC has also acquired one of the largest privately owned multi-family home building firms in the nation. In addition, GSC recently acquired 50.2 percent interest in a Dallas-based firm that manufactures computer hardware.

Penphil and Penn Central Purchase GSC Stock

On July 18, 1963, the Penphil Company purchased 10,000 shares of GSC common stock at $16.50 a share for a total investment of $165,000. On the same date, Penn Central purchased 4,000 shares of

GSC common stock at the same price as that paid by Penphil. This increased the Railroad's holdings of GSC stock at that time to 5,200 shares—the initial purchase of 1,200 shares was made in January 1963 at a price of $18.25 per share.

Penn Central continued to acquire GSC common stock and by July 1964 had acquired direct majority control of the Corporation. During this period of acquisition of GSC stock by Penn Central, Penphil maintained its interest in GSC. It was not until December 7, 1965, approximately 17 months after Penn Central acquired direct control of GSC and almost three years after Penn Central's initial investment in GSC, that Penphil sold its 10,000 shares of GSC stock.

Penphil Involvement with GSC

During the period of time it held its investment in GSC common stock, Penphil had numerous tie-ins with GSC, Penn Central and Glore Forgan, as described below:

1. Angus G. Wynne, Jr., a principal stockholder, director and officer of GSC was a principal stockholder in Penphil. Subsequently Mr. Wynne became a director of Arvida Corporation, another real estate development company controlled by Penn Central.

2. According to Thomas Bevan, Penphil's investment in GSC was made on the basis of recommendations by Hodge, David Bevan, and Haslett (Bevan's assistant at Penn Central), among others. Penn Central's purchases of GSC stock were made by David Bevan on the basis of his and Hodge's recommendations.

3. Charles Hodge had been affiliated with GSC since its inception and had a considerable personal investment in the firm. (His direct personal investment totalled about 38,000 shares as of June 12, 1970.)

In testifying before the CAB in November 1966, Hodge stated with respect to GSC as follows:

> I have (been) in that company since it started, and they asked me to find a good partner, owner, and that was the second (company) that the Pennsylvania Railroad acquired.
>
> *   *   *   *   *
>
> Q. And I gather through your association with Great Southwest, you personally were involved in that acquisition?
>
> A. Yes, I was. I was on the board.

4. In addition to Hodge's personal involvement, his company—Glore Forgan—served a dual role throughout the investment period. Glore Forgan served as the investment adviser to Penn Central and, at the same time, served as the investment banker for GSC. Penphil's purchase and sale of GSC common stock was made through Glore Forgan. Almost all of Penn Central's purchases were made through Glore Forgan.

5. Glore Forgan and several of its present and former officers and/or directors held substantial financial interests in GSC at June 12, 1970, as indicated below. The exact date on which these shares were acquired was not available. However, a substantial portion of these shares, according to the minutes of a December 6, 1963, GSC Board of Director's meeting, were acquired in 1963.

Shares of common stock held at June 12, 1970

Glore Forgan, Wm. R. Staats, Inc	62,000
Charles J. Hodge	38,000
J. Russell Forgan	38,000
Maurice H. Stans	38,000
Richard H. Millar	38,000
John F. Fennelly	37,400
Gerald T. Hodge	10,500
Other officers and directors	162,700
Total shares	424,600

6. Several members of Penphil, as detailed below, also held financial interests in GSC at June 12, 1970. In most instances, information was not available as to when these shares were acquired.

Shares of common stock held at June 12, 1970

Angus G. Wynne, Jr.[1]	326,300
Warren H. Bodman	2,000
Thomas R. Bevan	225
William R. Gerstnecker[2]	1,000
Samuel A. Breene	100
Vincent G. Kling	2,500
Total shares	332,125

[1] Mr. Wynne's holdings apparently were acquired when GSC was first incorporated.
[2] Mr. Gerstnecker has stated that his shares were acquired in 1970.

7. At the time of the initial Penphil and Penn Central purchases of GSC common stock, Charles Hodge and Angus Wynne, Jr., were members of the GSC Board of Directors. Both individuals were also principal officers of GSC at that time.

Once Penn Central acquired control of GSC in July 1964, David Bevan and William Gerstnecker became members of GSC's Board of Directors. Stuart Saunders, Chairman of the Board of Penn Central, also became a member of GSC's Board of Directors at the same time.

8. At the time Penn Central acquired control of GSC, the GSC Executive Committee consisted of seven members, including Charles Hodge and Angus Wynne, Jr. This was immediately reduced to five members, with Bevan and Saunders joining Hodge and Wynne on the Committee. The Executive Committee was reduced to four members in early 1965. The four members were all associated with Penn Central and/or Penphil—Bevan, Hodge, Wynne, and Saunders.

Once the Executive Committee became dominated by the Penn Central-Penphil group, it assumed a much greater role in the operations of GSC. At the same time, the role played by the Board of Directors of GSC decreased substantially. These changes in the roles of the Executive Committee and the Board of Directors are dramatically reflected in the minutes of the GSC Board and Executive Committee meetings.

Penphil Sells Its GSC Stock

In December 1965, seventeen months after Penn Central acquired control of GSC, Penphil sold its 10,000 shares of GSC stock. The sale was made through Glore Forgan. On the same date, Penn Central purchased 10,100 shares of GSC stock. The purchase was also made through Glore Forgan. Mr. Haslett informed staff investigators that the shares purchased by Penn Central included the Penphil stock.

Penphil sold its stock for $37.75 per share, for a total of $377,500. Penn Central purchased its shares on that date for $38.18 per share.

Penphil realized a profit of $212,500 on its GSC stock transactions, as follows:

Total proceeds from sale	$377, 500
Less: Cost of stock	165, 000
Profit on Sale of Stock	$212, 500

Conflicts-of-Interest?

The Penphil-Penn Central-Glore Forgan involvement with GSC raises very serious questions concerning real and potential conflicts-of-interest. The relationships that existed among Penphil, Glore Forgan, Penn Central and GSC afforded the members of Penphil and Glore Forgan the following opportunities:

1. Access to insider information through the interlocks that existed on the Board of Directors and the Executive Committee of GSC.
2. Control over the activities of GSC through the interlocks on the Board, the Executive Committee and the officer positions held by Wynne and Hodge.
3. The maintenance of the market for GSC stock by virtue of the vast amount of Penn Central financial resources available to David Bevan for purchasing GSC stock.
4. A ready buyer—Penn Central—in the event they wished to dispose of their GSC holdings.

David Bevan's Position

In a July 21, 1970, letter regarding the question of conflict-of-interest, David Bevan denied the existence of any such conflict.

> At the time we bought a small amount of Great Southwest stock for our [Penn Central] Contingent Compensation Fund, Penphil bought another odd lot offering with the same idea in mind that it was an interesting speculation.
>
> At that point, control of Great Southwest was tightly centered in the Rockefeller and Wynne families. No one had any possible way of knowing that at a later date a rift would occur in the Wynne family. However, this occurred in the following year and as a result Toddy Wynne, Angus Wynne's uncle, thereupon expressed a desire to dispose of the family's interest in Great Southwest. Since the understanding between the Rockefellers and the Wynnes was that they would act in concert, control of the company became available and it was offered to us through Glore Forgan and, of course, as you know we purchased controlling interest.
>
> A few months later I expressed a desire that Penphil sell its Great Southwest stock so that we would be sure to avoid any future possible conflict of interest. My wishes were respected and the stock was sold at a price of $38. All members of Penphil made a sacrifice in this connection as the price of $38 compares with even today's very low price of approximately $60 a share since the stock was later split 10 for 1. Actually at its highest the stock sold at $430 a share which was just a little over a year ago.

While Mr. Bevan makes his denial very emphatic, he fails to point out several pertinent facts.

1. The "few months later" was actually 17 months. It took Mr. Bevan that long to recognize the existence of a possible conflict of interest?

2. Mr. Bevan states that the members of Penphil "made a sacrifice" in selling the stock in light of the subsequent increase in the value of the stock. Mr. Bevan fails to explain how he could foresee the subsequent rise in the stock's value at the time Penphil sold. Also, it should be noted that if Penphil had held on to its stock, its value today would be considerably less than $38 a share.

3. The fact remains that the price obtained by Penphil for its stock—$377,500—represented a profit of $212,500. In percentage terms, Penphil investors realized about a 130 percent profit on their initial investment of $165,000, in a time span of less than 29 months.

4. Penphil acquired its stock in July 1963, at a price of $16.50 per share. From that time until Penn Central acquired control of GSC in July 1964, the per share price of GSC stock never rose above $24.

For about a year thereafter, while the Penphil ownership of GSC stock clearly created a conflict of interest, the price per share of GSC stock hovered around $19–$22. At no time during this one-year period did Mr. Bevan mention a possible conflict of interest and recommend selling Penphil's shares of GSC.

Beginning in August 1965, however, the price per share of GSC stock began to rise dramatically. By December 1965—less than 5 months later—GSC stock was selling for over $38 a share, a 73 percent increase in value. It was at this point that Mr. Bevan recognized the possible conflict of interest that resulted in Penphil selling its shares for a 130 percent profit.

5. The price per share obtained by Penphil in December 1965—$38—was 14 points higher than the previous high price of GSC stock since its incorporation through December 31, 1964; only 1½ points lower than GSC's high price for 1965; only 7½ points lower than GSC's high price for 1966; and only 7 points lower than GSC's high price for 1967.

It was not until 1968 that the price per share of GSC stock showed any significant increase over what Penphil received for its shares in December 1965. Accordingly, Penphil would have had to hold its stock for at least two more years before it could have realized any appreciable increase over the price it received in December 1965.

6. As detailed above, the Penphil sale of stock in December 1965 was very advantageous to Penphil stockholders. By waiting seventeen months to determine that a potential conflict of interest existed, David Bevan was able to obtain a very favorable price for Penphil's shares of GSC.

GSC Epilogue

After acquiring control of GSC in July 1964, Penn Central continued to acquire GSC stock. By December 1969, Penn Central had acquired over 90% control of GSC for a total investment of almost $92 million, an investment that still exists today.

In January 1971, GSC announced that it had written down its net worth from $157 million—its book value as of December 31, 1969—to a current value of $50 million. This represented a more than two-thirds reduction in the net worth of GSC.

In light of the above, Penphil's sale of GSC stock in December 1965 appears even more lucrative. Had David Bevan exercised the same business acumen on behalf of the Penn Central regarding its investment in GSC, Penn Central would not find itself in its current position of holding a $92 million investment in a $50 million corporation.

TROPICAL GAS CO., INC.

Between September 1, 1963, and September 29, 1963, Penphil purchased a total of 10,000 shares of Tropical Gas stock at a total cost of $191,495. The shares were subsequently exchanged for 8,900 shares of U.S. Freight Company stock when Tropical merged with U.S. Freight in October 1969.

Starting on February 26, 1960, and ending October 15, 1968, the Penn Central purchased a net total of 89,400 shares of Tropical at a total cost of $2,239,441. These shares were exchanged for 79,566 shares of U.S. Freight Co. stock following the merger in October 1969.

As of October 15, 1968, the combined holdings of Tropical stock by Penphil and Penn Central had reached a total of 99,400 shares at a ime when there were about 1.1 million shares of Tropical stock outstanding. Thus, Penphil and Penn Central collectively held almost 9 percent of the outstanding shares of Tropical Gas. The following paragraphs will make it clear, however, that the influence Penphil could muster over Tropical far exceeded the power Penphil could exert based strictly on the substantial combined stockholdings.

Both Penphil and the Penn Central were acting on the advice of Charles Hodge when the Tropical investments were made. That Hodge was well acquainted with Tropical is obvious from the fact that he and a former Glore Forgan partner, Alfonso Manero, have been directors of Tropical since 1954. Glore Forgan was the investment banker for Tropical and the investment advisor to Penn Central. In addition, David Bevan became a member of the Tropical board in 1964, the year following Penphil's final purchase of Tropical stock.

By early 1969, the membership of Tropical's Board of Directors and the stockholdings of those individuals in the company were as follows:

1. Fred H. Billups, (now deceased), Chairman of the Board, President and Chairman of the Executive Committee of Tropical; President and Director of Subsidiaries of Tropical; 51,610 shares.
2. Harry Hood Bassett, Chairman of the Board of the First National Bank of Miami; Chairman of the Board of First National Bank of Palm Beach; 6,000 shares.
3. David C. Bevan, Chairman of the Finance Committee and Director, Penn Central Transportation Company; 160 shares.
4. Edward F. Clark, Jr., partner in the law firm of Carter, Ledyard and Milburn; Secretary of Tropical and Director and Secretary of Subsidiaries of Tropical; 51 shares.
5. James E. Dingman, former Vice Chairman of American Telephone and Telegraph Company; Director of Communications Satellite Corporation, Triangle Industries, Inc., Gulton Industries and other companies (no stock).
6. Ralph W. Halsey, Jr., partner Halsey Associates, an investment advisory company; previously Associate Treasurer of Yale University; 10,800 shares.

7. Charles J. Hodge, Chairman of the Executive Committee and a Director of the investment banking firm of Glore Forgan, Wm. R. Staats, Inc., and partner of its predecessor, Glore, Forgan & Co; Vice President and Chairman of the Executive Committee of Tropical and Director of subsidiaries of Tropical; 9,544 shares.

8. Alfonso Manero, retired Vice President of Glore Forgan, Wm. R. Staats, and partner of its predecessor, Glore Forgan & Co.; 3,491 shares.

9. Hobart C. Ramsey, former Board Chairman of Worthington Corp.; Director of Armstrong Cork Co. and Triangle Industries Ramsey is also a former Glore Forgan vice president; 6,100 shares.

10. John Hagel, Jr., Executive Vice President of Tropical since November 1966; for more than four years prior thereto, general manager of Mobil Oil Caribe, Inc., San Juan, Puerto Rico; 4,196 shares.

Of the ten persons on the Tropical board in early 1969 (there was one vacancy), five—Billups, Bevan, Hodge, Manero and Ramsey—were Penphil shareholders. In addition, these five individuals comprised the complete membership of the Executive Committee of Tropical.

Tropical also had borrowed a total of $2.5 million from Harry Hood Bassett's bank, the First National Bank of Miami, and Tropical funds were deposited in that bank, which was the custodian of the company's stock purchase plan. As discussed later in this part of the staff report, First National of Miami had made a number of construction loans to Arvida, which is controlled by the Penn Central, had loaned the Pennsylvania Company $3 million to aid it in purchasing Arvida stock, and had loaned the Penn Central $1 million to cover commercial paper. Thus, the willingness of Bassett and First National to assist the leadership of the Penn Central, which was the leadership of Penphil, is well illustrated.

All of this boils down to the fact that from the time Bevan joined Tropical's board, Penphil was in a position to control Tropical through mutual alliances existing between six of the ten board members and through the combined private stockholdings of the six, together with the stockholdings of Penphil and Penn Central. These combined holdings, in early 1969, totaled 176,305 shares of Tropical stock and constituted 15.74 percent of the outstanding shares of Tropical common stock.

In addition, Tropical had a director interlock with Kaneb Pipe Line Company—Ralph W. Halsey, Jr., who was a director of Tropical since 1958 and held 10,800 shares of Tropical stock, and was also a director of Kaneb since 1958.

Of Penn Central's total Tropical stockholdings of 89,400 shares, 35,400 were purchased between September 20, 1968, and October 15, 1968, at a cost of $1,016,374. In effect, Penn Central increased its Tropical holdings by almost 40 percent in one 25-day period.

In the process, the price per share of Tropical stock was forced up nearly 20 percent, from $27.32 to $32.47 a share during this same 25-day period.

The purchase of Tropical stock during this period should be viewed against the following facts:

1. Penphil was in a position to control Tropical.

2. Between March of 1967 and September of 1968, Tropical's investment banker, Glore Forgan, prepared studies and proposals for financing Tropical's growth and expansion. On July 17, 1968, and on September 25, 1968, Tropical's board considered a specific plan for equity financing and authorized filing a registration statement with the Securities and Exchange Commission (SEC) for the sale of 230,000 shares of common stock.

3. Both Bevan and Hodge, as members of Tropical's board of directors and its executive committee, were aware of these studies and the decision to sell additional stock.

4. On October 2, 1968, Mapco, formerly the Mid America Pipeline Company of Tulsa, Oklahoma, announced that it would make a tender offer for all shares of Tropical to effect a merger with Tropical in which Mapco would be the surviving corporation.

5. Between October 3, 1968, and October 15, 1968, Penn Central purchased 9,800 shares of Tropical at a cost of $316,854.

6. On October 15, 1968, the date of the last Penn Central purchase of Tropical stock, Tropical publicly announced that it had filed its registration statement regarding the sale of the 230,000 shares of common stock with the SEC.

These dates comprise some of the milestones in what developed into a bitterly fought, prolonged and ultimately successful effort on Tropical's part to prevent a takeover by Mapco. During the course of the proceedings, a law suit was filed against Tropical by Mapco, and Tropical, in order to avoid presenting Mapco with the opportunity for strengthening its Tropical holdings beyond the 301,000 shares it had already acquired, withdrew the proposed 230,000 share stock issue and instead made a private sale of 122,000 shares to the Hillman Land Company of Pittsburgh, Pennsylvania, on January 9, 1969. The stock cost Hillman $3.7 million. The sale was arranged by Hodge, with the understanding that Hillman was making the purchase for investment purposes and did not intend to resell the stock. The purchase agreement with Hillman provided Hillman "piggyback" rights to join in any registered offering of Tropical's securities which Tropical might make, in each case without cost to Hillman except for any underwriting discounts or commissions involved. In October 1969, Tropical merged with and became a wholly-owned subsidiary of U.S. Freight Company of New York, and Mapco withdrew its law suit.

The paramount question arising from these transactions as far as Penn Central is concerned is why the Railroad, beginning on September 20, 1968, embarked on a campaign to purchase large amounts of Tropical stock when the chief financial officer and the chief investment advisor of Penn Central, namely Bevan and Hodge, knew well beforehand that Tropical would be making a large capital stock offering shortly thereafter which would, at least initially, dilute the earnings and the voting strength of all previous shares outstanding, including stock already held by Penn Central itself.

This same question was raised by investigators employed by the Penn Central Board of Directors early in 1970 to examine the validity of complaints raised by a stockholder, George J. Franks of Miami, as to whether the membership and activities of Penphil placed David Bevan in a conflict-of-interest position. Robert Haslett, then Penn Central Vice President of Investments, in replying to a query from the railroad investigators on July 28, 1970, wrote:

> The New York Central Pension Fund was merged into the Penn Central Pension Fund in May 1968, enlarging the funds by over $130,000,000. In view of the fact that Tropical was a major holding prior to the merger of the two funds, we decided to increase our commitment when stock became available with the idea of bringing the total to approximately 100,000 shares. * * *
>
> * * * Tropical was usually a difficult stock to purchase. * * *
>
> Between September 20, 1968, and October 15, 1968, we purchased through Glore Forgan 35,400 shares. * * *

Penn Central's largest single day purchase of Tropical stock was 18,000 shares made on September 20, 1968. Haslett told staff investigators that he received a telephone call from the Glore Forgan offices in New York on that day informing him of the availability of this stock. With Haslett's authorization, Glore Forgan purchased the shares.

During the period that Penn Central purchased the 35,400 shares of Tropical, on October 2, specifically, Mapco, Inc., announced plans to acquire Tropical Gas through an exchange offer of nine-tenths of a share of Mapco for each share of Tropical. At that time Mapco was selling at 37 per share and Tropical was selling at 32 per share.

Mr. Haslett further stated in his letter:

> Our last purchase of stock was on the 15th of October. The following day the company officially filed a Registration Statement for the sale of 230,000 additional shares of common stock. This was the first knowledge I had of any proposed financing, and, as a result, no further purchases were made.

Haslett was saying in effect that Bevan and Hodge revealed nothing to him of the pending sale of 230,000 shares of Tropical prior to the filing of the registration statement by Tropical. Evidence that Hodge was well aware of the proposed sale is contained in a letter dated August 16, 1968, from Billups to John Hagel, Jr., an Executive Vice President of Tropical. The letter was written 25 days before Penn Central began picking up the 35,400 shares of Tropical stock.

It reads in part:

> As you already knew * * * we planned on and have already begun a company-wide audit through Price Waterhouse as of July 31, 1968. Immediate action in this regard was necessary because of the strong recommendation of Jack Harned [of Glore Forgan] with the concurrence of Charlie Hodge, that the issue of the stock to the public be made the earliest date possible in order to take advantage of the present general market which they have reasons to believe might decline further. This audit is being undertaken in the most expeditious manner possible. * * *

The foregoing material makes the following apparent.

Penn Central, beginning on September 20, 1968, began purchasing large amounts of Tropical stock in the market, despite the fact that Bevan and Hodge knew that the earning power and, therefore, the value of these shares would be diluted with the sale of Tropical's new stock issue of 230,000 shares—indeed, despite their knowledge that the value of all existing Tropical shares would be diluted with the sale of the new stock. The same situation would apply to the voting power of all existing stockholders unless the Penn Central acted beforehand to increase its holdings as a buffer against the broadened stockholder base resulting from the sale of the new issue. In other words, while all other existing stockholders would tend to lose strength in Tropical, Penn Central's position would remain relatively unchanged and might be materially enhanced because of the large blocks of stock it was purchasing in the period just before the proposed new stock issue was filed with the SEC.

It was to Penphil's advantage not to purchase stock during this period because Bevan and Hodge knew the value of all stock would go down. By the same token, it was to Penphil's advantage to let Penn Central take the loss, knowing that it (Penphil) could maintain its control position over Tropical through Penn Central's strengthened voting power.

When questioned by staff investigators, Haslett was unable to give a clear-cut answer when he was asked why the Penn Central waited 173 days after the merger of the New York Central and the Pennsylvania Railroad pension funds before purchasing large blocks of Tropical stock.

"Tropical was a very lightly traded stock", Haslett said. "Maybe we just didn't get around to it before then. Anyway, we didn't want to have to buy the stock in small amounts." This last was a reference to the purchase of 18,000 shares of Tropical on September 20, 1968, the day the Penn Central began its campaign to enlarge its Tropical holdings to 100,000 shares. However, a document tracing the history of Penn Central's Tropical purchases shows 15 instances both before and after September 20, 1968, when the railroad bought small blocs of Tropical stock ranging from 83 to 3,000 shares.

Haslett said that he did not know the identity of the owner or owners of the 18,000 shares that Penn Central purchased in one day, an unusual transaction for Tropical stock, inasmuch as monthly trading ranged between 10,000 and 25,000 shares from May 1968 to August 1968. He added that he did not make any effort to find out who had owned the stock.

"Normally," Haslett added, "Dave Bevan was aware of Penn Central's Tropical stock purchases, but I'm not sure if he was in this instance [the purchases made between September 20, 1968, to October 15, 1968]."

When asked whether he thought Bevan and/or Hodge should have informed him about the pending sale of 230,000 share of additional stock by Tropical, Haslett replied, "Would that not be inside information?" Haslett was then asked whether he thought Bevan's responsibility to protect the interests of the Penn Central was greater than his responsibility to Tropical. "I don't know which one he had a responsibility to first. I just can't answer that," Haslett told staff investigators.

There is another aspect of the Tropical-Penn Central stock situation which raises questions concerning the propriety of Penn Central's purchases of Tropical stock in the fall of 1968. The following information was developed after staff investigators had interviewed George F. Bennett, President, State Street Investment Corp., Boston: Allen Chandler, a petroleum analyst for the State Street Research and Management Corporation, Boston (an affiliate of the State Street Investment Corp.); Robert E. Thomas, president of Mapco, Inc., of Tulsa, Oklahoma; and Herbert E. Fisher, Chairman of the Board of the Kaneb Pipe Line Company and a Penphil shareholder. (Penphil holds 30,488 shares of Kaneb and the Penn Central holds 122,500 shares of Kaneb.)

During the late winter or early spring of 1968, Chandler said he contacted Thomas and told him there was "an excellent acquisition opportunity for Mapco." Chandler said he knew of three institutional investors which held Tropical stock and were "disenchanted" with Tropical's growth and management. The three institutions were the State Street Investment Corporation, Harvard College and Yale College. Together they held 301,000 shares of Tropical stock. In addition, State Street Investment Corp. held 135,900 shares of Mapco stock.

Thomas and Chandler said that from time to time, beginning in the late winter or early spring of 1968, Thomas discussed the possibility of exchanging Mapco stock for the Tropical shares held by the three institutional investors as part of Thomas' effort to effect a merger of Tropical and Mapco, with Mapco being the surviving corporation. Chandler told staff investigators that during this period, a Tropical director (identified by Bennett as Joseph J. Snyder, Vice President and Treasurer of the Massachusetts Institute of Technology) invited Billups, President of Tropical, to come to Boston to meet informally with representatives of the three institutional investors. The meeting was held May 29, 1968, in the Ritz Hotel in Boston, Chandler said. Chandler recalled that the discussion with Billups centered on plans for the operation and future growth of Tropical and that Thomas' activities to obtain Tropical stock as part of his merger effort was not mentioned during the meeting. At the time, Chandler said, the three institutional investors were dissatisfied with Billups' leadership of Tropical because they thought the growth of its stock was too slow, management was too conservative and Billups was running the corporation "like it was his personal empire." Billups' income from Tropical, amounting to $108,000 in 1968, retirement benefits of $50,000 a year, plus survivors benefits of $300,000 in the event of his death, figured in the dissatisfaction of the three institutional investors, who thought these were excessive sums for such a relatively small corporation, Chandler said.

On October 2, 1968, Mapco issued a press release announcing that:

> A tender offer for all the shares of Tropical Gas Company, Inc., is to be made by Mapco, Inc., as soon as the necessary registration statement can be filed and become effective. Mapco will offer nine-tenths of a share of Mapco common in exchange for each Tropical share now outstanding. A ruling will be requested from the Treasury Department and the exchange is expected to be tax free. Mapco has commitments to accept such an offer from the holders of 301,000 Tropical shares [the three institutional investors] and informal indications to accept an additional 80,000 shares.

The tender offer was predicated on its acceptance by the holders of 80 percent of the outstanding Tropical stock.

On October 3, 1968, the following day, a special meeting of the Tropical board was held with Billups, Hodge, Bevan, Ramsey, Halsey and Clark present. The minutes of that meeting read in part:

> Mr. Billups told the board that the meeting had been called on short notice to consider the bid by Mapco, Inc., to take over this company.
>
> He had learned of this proposal, he said, late in the afternoon of the previous day through the financial press, without notice from Mapco of any kind. He had declined comment on the proposal until the board could be assembled for consideration of the matter and information could be collected concerning Mapco and its offer.
>
> Mr. Harned [John Harned, former senior vice presdient of Glore Forgan] presented an analysis of Mapco's financial position and an investment banking analysis of the proposed transaction, which he thought

> disadvantageous to Tropical. Mr. Bevan, agreeing with the analysis, gave his opinion of Mapco's condition and prospects, and the probable value of its stock. * * *

During the meeting, a resolution was adopted stating the board's opposition to the exchange offer.

The minutes of the meeting also contain the following paragraph:

> Mr. Hodge advised the Board that he had discussed Mapco's offer with Mr. Snyder, who could not be present at the meeting, and that Mr. Snyder had advised that he was opposed to the acceptance offer. * * *

In a letter dated October 11, 1968, mailed to Tropical shareholders, the company's board of directors set forth their reasons for opposing the Mapco exchange offer. The following pertinent excerpts are quoted from that letter:

> Since well over 20 percent of Tropical's common stock is owned by your Company's officers and directors, and members of their families and by other stockholders who have already advised management that they would reject the Mapco offer, the exchange could not be 'tax free'—a condition of the offer.
>
> Even though earnings per share of Tropical have been higher than those of Mapco in every year for the past eight years, Mapco proposes to offer only 9/10's of one of its common shares for each share of Tropical.
>
> Mapco is heavily burdened with debt. Its prospectus dated April 17, 1968, showed total long term debt of approximately $98,000,000 of which more than $17,000,000 was incurred subsequent to the beginning of the year. This indebtedness was 70 percent of its total capitalization as compared with common stock equity of only 21 percent with convertible preferred stock accounting for the balance. In contrast, Tropical's capital structure [as of] July 31, 1968, included 37 percent long term debt ($8,185,000) and common stock equity of 60 percent with preferred stock accounting for the balance.
>
> Mapco will have debt maturities aggregating $25,000,000 in 1969 and 1970. The necessity for refinancing so large a part of its total capitalization in two years could subject Mapco to severe financial pressure.
>
> The interest costs on Mapco's debt in 1967 totalled $6,527,000 or 10.3 percent of Mapco's total revenues of $63,589,000. By comparison, Tropical's 1967 interest costs were $635,000 or 2.9 percent of total revenues of $22,274,000.

When he was questioned by staff investigators, Haslett said he continued to authorize the purchase of Tropical stock for the Penn Central after the October 2, 1968, tender offer announcement "because the takeover price made Tropical stock appear cheap." He added that he was not concerned about whether Mapco succeeded in its effort to take over Tropical. He also said, "I was not aware that Penn Central purchases of Tropical stock were driving the price up."

As indicated earlier in this section of the report, Billups and the Tropical board made a point of noting that they were not aware of Mapco's intentions prior to that company's October 2, 1968, press release. When questioned about this, Thomas told staff investigators that he packaged the entire Mapco takeover attempt very quickly. He stated that he (1) obtained assurances from the three institutional investors that they would be willing to exchange their 301,000 shares of Tropical for Mapco, (2) obtained the consent of Mapco's executive committee to make the tender offer announcement, and (3) authorized issuance of the press releases—all within a single 24-hour period ending on October 2, 1968.

Thomas said that he had not spoken with Billups at any time during the period leading up to the October 2 announcement, although he tried to telephone Billups at his office and at his home on October 2 just prior to issuance of the press release concerning the tender offer announcement. Thomas said he was told by Billups' office that Billups was at his home. He said he then telephoned Billups' home where the call was answered by Mrs. Billups. Thomas said there was a long pause after he asked to speak to Billups during which he overheard conversation involving a male voice in the background. Presently, Mrs. Billups returned to the telephone to say that Billups was not home.

The question arises that if Billups were at home at the time, why would he refuse to talk to Thomas, unless he already knew of Thomas' plans to try to effect a Mapco takeover of Tropical?

All of this was said by Thomas in discussion of the question of whether Billups had prior knowledge of Mapco's intention to effect a merger with Tropical. Thomas asserted that he was certain that Billups was aware of this effort. When asked to explain, he replied that he understood that Snyder was working quietly behind the scenes to arrange the merger on the most amicable basis possible and therefore he, Snyder, must have spoken to Billups about the matter.

To questions as to why he did not attempt to contact Billups before October 2, 1968, to try and make arrangements for a merger on a mutually agreeable basis, Thomas said that he had expected Billups to resist the merger effort and therefore the element of surprise was all important. "The way to do these things," Thomas said, "is to move quickly."

Snyder was contacted in connection with Thomas' statement, and the following exchange with staff investigators took place:

Q. When were you first aware of the merger?

A. I would have to look at the record. I am not that close to it now. I am not really clear about that . . . I did have some information that there were discussions going on with Mapco. I am not sure who was interested in Tropical—who was discussing this with Mapco and Mr. Thomas.

Q. Did you discuss this with Fred Billups?

A. Do you mean formally?

Q. Well, informally?

A. I did not talk with Fred Billups.

Q. Do you have any recollection of when Mr. Billups or the Tropical Board became aware of Mapco's intentions?

A. I am afraid you are putting questions to me I couldn't answer that realistically.

Q. Do you have any records—a diary?

A. I did not keep such a thing. I was out on the edges of this thing and not really that closely involved.

Q. Is Mr. Thomas' description of your attitude concerning the merger accurate?

A. No, I wouldn't say that. I think it was more concern on my part if there was any friendly way to do this rather than a combative way. And that was my only concern.

In effect, this is the attitude that Thomas said was held by Snyder concerning the merger.

In this connection, there is an interesting reference to Snyder in the minutes of a special meeting of the Tropical board on November 20, 1968:

> After referring briefly to operational developments, Mr. Billups opened the meeting to discussion of the offer by Mapco, Inc. to purchase from the company for cash at $32 per share the 230,000 shares of Tropical Common Stock now in registration with the SEC.
>
> Mr. Snyder informed the meeting that he felt he should resign from the Board of Directors on advice of counsel in order that the Massachusetts Institute of Technology, whose stockholdings in Tropical he represented

> on the board, might be free to sell all or part of its shares if it so desired, without suspicion that it had acted on inside information obtained from him as a Director. He added that MIT had not at present any plans to sell its Tropical stock to Mapco, Inc. or to anyone else. After discussion, it was agreed that Mr. Snyder would postpone his resignation at least until further consideration had been given concerning it [until] after the meeting but in the meantime he would not vote or be recorded as voting on any matters coming before the meeting.

Snyder did resign from the Tropical board and was replaced by M. J. Rathbone, a director of Executive Jet Aviation, in early 1969.

The rationale given for Snyder's resignation from the Tropical board is puzzling. He was reportedly saying in effect that he wished to resign so that MIT could sell its Tropical stock without complication, yet MIT, at the time, had no intention of doing so. Snyder's resignation from the board and the reason given for that resignation were viewed by staff investigators against an assertion made during the investigation by Stuart Patton, a Miami attorney who represented Tropical when it was sued by Mapco. Patton told staff investigators that during the discussion between Thomas and the three institutional investors George Bennett, President of State Street Investment, told Thomas that he was prepared to bring into exchange for Mapco shares the Tropical stock held by Yale, Harvard and State Street and that he thought an exchange arrangement could also be made with MIT and Northwestern Mutual Life Insurance Company, which also held large blocks of Tropical stock. The deal for the MIT and Northwestern Mutual stock, Patton said, never went through.

When contacted by staff investigators, Bennett stated that he had asked Snyder to arrange the May 29, 1965, meeting between Billups and the three insitutional investors. Bennett said he also talked to Synder prior to the announcement of October 2, 1968, in an effort to persuade Snyder to support Thomas' merger effort. Bennett said, "Joe listened but said nothing to indicate his position. This, of course, was to be expected inasmuch as he occupied an insider position."

The conversations between Thomas and the three institutional investors, the meeting of these investors with Billups during the months leading up to Mapco's announcement of its intention to make a tender offer to effect a merger with Tropical, and Thomas' unsuccessful efforts to contact Billups by telephone all give rise to the question as to whether Billups and other members of the Tropical board, namely Bevan and Hodge, knew of Mapco's intentions before Mapco's public announcement on October 2, 1968. If Bevan and Hodge were aware of Mapco's plans before September 20, 1968, then this knowledge must be considered in connection with the Penn Central's heavy purchases of Tropical stock starting on that date. Just as Tropical later decided to withdraw its registration for public sale of 230,000 shares of common stock for fear it would be purchased by Mapco, so too would it be logical for the Penn Central-Penphil-Glore Forgan combine, which was in control of Tropical, to make large purchases of Tropical stock to prevent such shares from being taken up by Mapco, which would have resulted in the elimination of Penphil's control of Tropical.

Another mysterious aspect of the Mapco merger story involving Herbert E. Fisher, Chairman of the Board of Kaneb Pipe Line Co. of Houston, should be noted. Fisher is a Penphil member. Penphil holds 30,488 shares of Kaneb stock, and the Penn Central holds 122,500 shares of Kaneb. David Bevan is a member of Kaneb's Board of Directors.

Fisher told staff investigators that he had visited members of his family in Tulsa, Oklahoma, during the Christmas season of 1968. While there, he received a call from David Bevan who wanted Fisher's opinion of Mapco. Fisher told staff investigators that he was put out by such a call being made under the circumstances in which he found himself, but that Bevan insisted on getting his opinion. He said he told Bevan that he was not at his office and, therefore, could not refer to hard data on Mapco, but that he thought that Mapco was not in a sound financial condition. Fisher said he does not understand why Bevan would make a call to ask for his opinion on Mapco nearly three months after Bevan, Hodge and other members of the Tropical board had voted to oppose the Mapco takeover effort.

In this connection, it is interesting to note that Haslett, who was an assistant to Bevan, told staff investigators that he was not concerned about the prospect of Mapco taking over Tropical Gas. This in turn raises questions about whether Bevan had ultimately decided to play the odds and go with whatever force seemed strongest in the Mapco-Tropical battle.

Tropical Epilogue

Subsequently, in October 1969, Tropical Gas merged with and became a wholly-owned subsidiary of U.S. Freight Company. Billups and Hodge became members of the U.S. Freight Board of Directors. Billups died on May 15, 1970.

As a result of the merger, Penphil received 8,900 shares of U.S. Freight stock in exchange for its 10,000 shares of Tropical. Penn Central received 79,566 shares of U.S. Freight in exchange for its 89,400 shares of Tropical.

The new combined Penphil-Penn Central holdings in U.S. Freight Co.—88,466 shares—represented less than 1.3% of the outstanding stock of U.S. Freight Co. In addition, following Mr. Billups' death, Penphil had only one director interlock with U.S. Freight. Accordingly, the Penphil-Penn Central-Glore Forgan combine could not exercise control over the activities of U.S. Freight Company.

This situation should be noted in connection with the fact that the U.S. Freight stock was one of the two holdings sold by Penphil in the summer of 1970 in order to reduce the balance of its outstanding loans to Chemical Bank.

PENPHIL'S FLORIDA BANK INVOLVEMENT

Letter dated December 23, 1966, from Benjamin Sawin to Thomas Fleming, Jr:

> Confirming our conversation yesterday, there will be a wire transfer of $250,000 from the Chemical to the First Bank and Trust Company of Boca Raton on December 30. I have already asked Tom Bevan to work out the arrangements for availability of these funds as the rights and/or blocks of stock become available directly from Morgan Zook [then executive vice president, First Bank and Trust Company, Boca Raton.]
>
> This will also confirm our understanding that so far as possible the acquisition of stock will be on the basis of $200,000 for First Bank and Trust Company [of Boca Raton] and $100,000 for University National Bank [of Boca Raton] * * *

Letter dated January 10, 1967, from Thomas Bevan to Morgan Zook:

> Enclosed is a certified copy of resolutions and signature cards covering the Escrow Account of Penphil Co. in your bank. This morning I talked to Chemical Bank of New York and arranged to send $50,000 as additional funds for this account.
>
> This will also confirm my statement to you over the telephone authorizing the purchase of shares of University Bank at $20 per share.

With this transaction, Penphil entered the Florida banking industry. By the end of 1968, the company held investments in the two banks costing $427,108. On September 1, 1970, the stock was valued at $1,244,852, constituting a paper profit of over 191 percent.

The breakdown of Penphil's investment in the two banks is as follows:

First Bank and Trust Company of Boca Raton, 21,380 shares costing $332,924 and having a market value of $964,772 on September 1, 1970.

University National Bank, 4,868 shares costing $94,184 and having a market value of $280,080 on September 1, 1970.

In addition, Penphil has joined with a group of Florida bankers, real estate dealers, contractors and lawyers in an effort to establish a new commercial bank at Deerfield Beach, Florida. Ultimately, Penphil was to have purchased a five percent interest in the planned lending institution, the application for which is still pending before the Comptroller of the Currency. So far, Penphil has invested $12,886 as its share of site acquisition costs and expenses.

On October 20, 1970, Thomas Bevan wrote to Fleming:

> This is to advise you that it will not be feasible for this company [Penphil] to pick up its commitment for the 5,000 shares of the proposed National Bank of Deerfield. Accordingly, we hereby release the incorporators of the Bank from the obligation to issue such shares and request that you return to us the $12,886.11 which this company paid to you in connection with acquisition costs and expenses.

Fleming told staff investigators that he has declined to return the money to Penphil because of what he said were heavy expenses in connection with the effort to establish the bank. He said it was his understanding that Penphil made the request because it needed this cash.

The man who was instrumental in drawing Penphil's attention to Florida banking investments was Benjamin F. Sawin, Chairman of the Board of Provident International, a division of the Provident National Bank of Philadelphia, where the Penn Central maintained major deposit and loan accounts. Bevan and Gerstnecker were on the Provident National Bank's Board of Directors. In 1969, Gerstnecker was made Vice Chairman of the board. He resigned from that position in January 1971. One of the original 16 organizers of Penphil, Sawin has had a residence in Boca Raton for some years. During visits there he struck up a friendship with his fellow banker and neighbor, Thomas Fleming, Chairman of the Board both of First Bank and Trust and University National.

After conferring with Fleming, Sawin wrote a detailed memorandum on December 8, 1966, to the Penphil Acceptance Committee outlining the dramatic growth of Boca Raton, Broward and Palm Beach Counties by way of setting forth a rationale for Penphil's investment in the two Boca Raton banks which serve the region. He pointed out that the population of Broward County had risen from 39,794 in 1940 to 500,400 in 1966, and that Palm Beach County had a population which rose from 78,989 to 320,000 during the same period. The population of Boca Raton, which is in Palm Beach County, went from 723 persons in 1940 to an estimated 17,900 in 1966. It was asserted that Broward was Florida's fastest growing county.

Sawin also noted that total deposits of First Bank and Trust and University National combined amounted to $26.7 million in 1966, compared with total deposits of $22.2 million in the Boca Raton National Bank, the only other commercial bank in town. Projections cited called for First Bank and Trust and University National deposits to increase to 52.8 million, or 54.6 percent of total bank deposits in the community by 1970.

The projections turned out to be on the conservative side. Polk's World Bank Directory of September, 1970, shows that the combined deposits of First Bank and Trust and University National totaled $66,335,240 and that their combined assets totaled $74,480,294. By comparison, Boca Raton National Bank had total deposits of $45,-171,041, and total assets of $50,222,612. In other words, First Bank and Trust and University held 58 percent of all commercial bank deposits and 59 percent of all commercial bank assets in Boca Raton in the middle of 1970. These figures make it clear that First Bank and Trust and University National have assumed a dominant position in commercial banking in the immediate Boca Raton area. Riviera Beach, the nearest community to Boca Raton, has two banks. These are First Marine Bank and Trust Company with assets of $46,781,151, and First National Bank and Trust Company with assets of $29,183,113, according to Polk's World Bank Directory of Septemper, 1970.

About midway through the December 9, 1966, memorandum, Sawin noted a sharp decline in First Bank and Trust deposits between 1964 and 1965, and commented:

> The downward trend might be explained in part at least by Mr. Fleming's activities on behalf of Lyndon B. Johnson in the last election when he acted as his Campaign Manager for the state of Florida. Boca Raton is a strong Republican community. I have discussed this matter with Mr. Fleming and he believes he has mended most of his fences and at the present time his past political activities are being forgotten.

The conclusion of the memorandum contains the following statement:

> In the event it is decided to proceed, and I have been unable to uncover any reason why we should not, Mr. Fleming is quite anxious to know as soon as possible so that we can conclude the negotiations and he can start accumulating First Bank and Trust stock, and more particularly the stock of University National where he expects to encounter more difficulty.
>
> If the Acceptance Committee desires to proceed, will you signify your approval on the copy attached so that I may immediately conclude negotiations with Mr. Fleming and also use this as authority for Tom Bevan to have the funds available so the stock can be accumulated.

The left bottom corner of the lást page of a copy of the memorandum contains the notation and signature, "Approved, Charles J. Hodge, Chairman, Acceptance Committee."

Although the memorandum did not mention this, it should be noted that the Arvida Corporation, 58.3 percent of the stock of which is owned by the Pennsylvania Company, owns and operates a large luxury resort facility, the Boca Raton Hotel and Country Club, and has made Boca Raton the site of a major real estate development project. These facilities and investments have a direct bearing on economic growth and prosperity in the area served by the two Boca Raton banks in question. Details on Arvida are given elsewhere in this report.

A few months later, in early 1967, Sawin was elected a Vice President of Penphil and about a year later the way was cleared for him to become a member of the Boards of Directors of First Bank and Trust and University National. The first item of the June 30, 1968 financial statement of Penphil declares:

> On February 20, 1968, the Executive Committee of the Board of Directors authorized the transfer to an officer and stockholder of the Company of 200 shares each of the capital stock owned by the Company, of First Bank and Trust Company of Boca Raton, National Association, and of University National Bank of Boca Raton, to be used as qualifying shares for membership on the Board of Directors of these banks. An agreement was executed to return said capital stock certificates to the company upon demand. The indebtedness to the Company has been valued at cost of the shares transferred.

In other words, it was at the will of Penphil that Sawin was serving as a director of the two Boca Raton banks and his position with these banks could be terminated simply by recalling the stock transferred to him. These circumstances automatically give rise to the question of whether Sawin felt his primary responsibility was to the banks or to Penphil.

Four months later, on June 3, 1968, Sawin wrote a memorandum to David Bevan proposing that Penphil expand its Florida bank holdings. Sawin stated:

> As you will probably recall, on several occasions during the past winter, I attempted to look into the situation as it concerned the Deerfield Bank, Deerfield Beach. I uncovered sufficient information to lose interest in acquiring it because of the rumored condition of some of its loans and the background of the people who controlled it. More recently, Morgan Zook has looked into the situation with the same conclusions.
>
> Concurrently with all this, another group has acquired a charter for a new national bank in Deerfield Beach. They represent a generally favorable reputation but no banking experience. Upon uncovering this situation and as several of the organizers were well known to Tom Fleming, he has talked them into a 35 percent interest of which he will keep 10 percent to 15 percent. The balance will be distributed in blocks of 5 percent each to Penphil and others known to him.
>
> It will be agreed that Bill Stowe [William M. Stowe, then President of and a director both of First Bank and Trust and University National Bank] will go down to start the bank out, which he is entirely capable of doing.

Fleming told staff investigators that Stowe was to be president and a director of the new Deerfield Beach bank.

The June 1968 Sawin memorandum continues:

> At Tom's suggestion the group also has an option on a piece of ground which in my opinion would represent just about the ideal location for a bank in Deerfield.* * *
>
> I would recommend that Penphil acquire at least the 5 percent tentatively allotted and more, if possible. The original capitalization will probably be about $1 million, so we would be thinking of a minimum $50,000.* * *

Sawin's memorandum also dealt with the financial needs of First Bank and Trust. He wrote:

For some time we have been aware of the eventual need for additional capital for the First Bank and Trust Company of Boca Raton, National Association. This has been evidenced by comments of the Bank Examiners as well as the very rapid growth in deposits. It has apparently come to the point now where something will have to be done. I have agreed all along with Morgan and Tom, particularly Tom, that we should keep ourselves out of a debenture position as long as we possibly could, which would be particularly true in this kind of market. Eventually, we may have to do a debenture job, but the larger the bank is obviously the better its credit will be, and so I would be hopeful this could be put off but that we could satisfy the Examiners with the issuance of more capital stock. If this matter comes up at the June Board Meeting, if possible, I will attend and will have more of the current thinking and detailed information. * * *

Will you kindly discuss this with the other members of the Executive Committee and advise me as to how much money will be available and how far you would care to go.

On June 5, 1968, David Bevan wrote the following letter to members of the Penphil Acceptance Committee, then consisting of Cannon, Haslett, Hodge, Horner and Stevens:

Enclosed is a copy of memorandum from B. F. Sawin. I would recommend that you accept his recommendations and that we go as far as we can in conjunction with these two items up to a total of $250,000.

If this is authorized, we will make sure ahead of time that this amount of money can be borrowed, but I think it is unlikely that we can invest probably more than $150,000 to $200,000.

Please let me have your reaction as promptly as possible.

Hodge replied on June 7, 1968:

With reference to your letter of June 5, 1968, and memorandum from Ben, I concur completely with Ben's recommendation and you have herewith my affirmative vote.

Sawin's memorandum and Penphil's response to it provides a fairly graphic description of the information pipeline Penphil had established inside the two Boca Raton banks. Sawin's memorandum also makes it difficult to resist the conclusion that any information he acquired that might be of any conceivable use to Penphil was promptly passed to Penphil.

That Sawin's role as agent for Penphil at First Bank and Trust and University National was known to senior officers of those banks is indicated by the following letter dated August 20, 1968, from Thomas Bevan to Zook.

I am enclosing herewith Warrant No. 319 in the name of Penphil Co. and Warrant No. 339 in Ben Sawin's name, which has been duly assigned to Penphil Co. These warrants cover 9,075 rights—or 1,815 shares.

You will find enclosed a check of Penphil Co. in the amount of $90,750.00, dated August 30, 1968, which I would appreciate your submitting—together with the warrants—to your Transfer Department on August 30 of this year.

The link between Penphil and the two banks became even stronger later in that year. A letter dated December 10, 1968, from David Bevan to Sawin, reads as follows:

Enclosed is a balance sheet of Penphil which you can show and go over with Tom Fleming. You will recall that we promised him an opportunity to participate at some point.

> As you know, we are offering all stockholders the right to subscribe to an additional 300 shares at $35 a share. Carroll Seward is liquidating his interest in Penphil at the same price since he is about to retire. At the present time he holds a total of 3,000 shares. Connie [Cornelius] Dorsey would like to acquire about 600 to 700 shares and Tom Fleming can have all or any part of the balance.
>
> The price of $35 was below the market at the time the circular was sent out to all members. I think the market value was about $37 a share. Without re-evaluation, I cannot tell you what it is now but there is a substantial rise. Our biggest holding is Kaneb and I would guess it would be $2 or $3 higher, so it represents a real opportunity and bargain price for Tom. We have to know promptly whether or not he wants in. If he does not we will just have the company [Penphil] buy the stock.

Fleming wrote to David Bevan on December 10, 1968:

> Ben Sawin showed me your letter of December 10 in which you advised that Mr. Carroll Seward is liquidating his interest in Penphil at $35 a share. Of the approximate 3,000 shares which he now holds, you stated that Connie Dorsey would like to acquire 600 to 700 shares and that I could have all or any of the balance at $35 per share.
>
> This is to advise you that I am thrilled and delighted and want to take all of the stock that is left. Therefore, I am making my plans to pay for 2300 or 2400 shares of stock.
>
> I am so happy to join this exalted group of gentlemen investors about whom I have heard so much. I want to thank you for this opportunity to join your group.

On December 23, 1968, Thomas Bevan wrote to Fleming:

> Dave has forwarded to me your letter of December 16, in which you expressed an interest in acquiring Penphil shares from Carroll Seward at $35 a share. I have talked to Connie Dorsey who wishes to acquire 715 shares, which would leave the balance available to you of 2,285 shares.
>
> Will you please advise me if you are still interested, and if so, when you can make payment on these shares.
>
> We will be delighted to have you as a member of our group and I hope I can see you the next time I am in Florida.

Fleming was indeed still interested and forthwith became a Penphil shareholder. In the process, based on David Bevan's estimates of the selling price and market value of the stock, Fleming made a paper profit of $11,425 the moment he became the owner of the stock.

Fleming told staff investigators that he thinks Sawin introduced him to the idea of becoming a Penphil member. Fleming asserted, "I wanted the stock because it meant something to be associated with these men." Apparently the association held appreciably less meaning to him after the collapse of the Penn Central because he told investigators that he agreed with the August 1970 decision (later rescinded) to liquidate Penphil. When asked why, he said, "I needed the cash."

Papers submitted to the staff by David Bevan make it clear that Fleming had invited Penphil to accept membership among a group which was intent on expanding their Florida bank holdings to include new investments on both coasts of the state. On February 5, 1969, Thomas Bevan wrote David Bevan:

> . . . I have received a call from Ben [Sawin] who had three items he wanted me to raise with you:
>
> 1. In two or three months we will need approximately $15,000 in connection with the real estate for the proposed Delray bank [in the next town north of Boca Raton]. Tom Fleming is trying to get this [bank approval] through Washington and it looks as if it will take some time.

2. Tom Fleming indicates that we have a chance to buy, with his group, a bank at Sarasota [where Arvida had real estate holdings] which will cost $3,000,000. Our share will cost approximately $300,000 representing 10 percent of the whole deal.

3. The Stock in the First Bank and Trust Company of Boca Raton has been split 2 for 1 and is now selling for $57, which is equivalent to $114 per share on the pre-split stock. He wants to know whether he should buy some more of this since it will become available because of having been split.

I have mentioned some of these things to Larry Stevens and Warren Bodman, so I think it would be wise to discuss this with the Investment committee. . . .

When he was questioned on these points, Fleming denied any knowledge of a proposed bank at Delray. He also indicated that the deal to purchase the Sarasota bank fell through.

In September 1969, Fleming publicly announced that the directors of the First Bank and Trust Co. of Boca Raton, University National Bank of Boca Raton, First National Bank and Trust Company of Riviera Beach and Citizens Bank of Palm Beach County had approved affiliation of their institutions with a proposed registered bank holding company, First Bancshares of Florida, Inc., of which Fleming would be Chairman of the Board. Thus, First Bank and Trust and University National joined the trend of creating registered bank holding companies—a trend that has come to dominate Florida commercial banking because it provides a mechanism by which Florida's prohibition against branch banking is being circumvented. Although all four banks are relatively small, their combined assets total $116.7 million a figure big enough to allow the four to collectively compete with much larger institutions in the surrounding area, including Palm Beach and Fort Lauderdale.

In the process of forming the new holding company, Sawin showed Penphil how he thought the company could save $100,000. On November 14, 1969, Sawin wrote to Thomas Bevan:

Pursuant to our recent conversations, particularly with Dave, it appears that it may be possible to pick up in the neighborhood of 10,000 shares of the First National Bank of Riviera Beach. . . .

It appears that if the acquisition can be made that the price will be somewhere between $55 and $60 per share, probably closer to the latter figure. . . .

As the agreed upon arrangement provided for a share per share exchange of the holding company for the banks involved, it appears that the possibility of being able to purchase the aforementioned shares of First National Bank of Riviera Beach at or around $60, as compared to the purchase of roughly a like amount of shares in the First Bank and Trust, would be a distinct advantage to our group.

Why don't you present the proposal to the finance committee on two bases.

#1—Authorize me to negotiate for the shares of the First National of Riviera Beach up to $60 a share and, if this is not possible and it well may be I cannot pick up the stock, then I would also like authorization to purchase, again if possible, up to 10,000 shares of First Bank and Trust at a price of $70.

Five days later, on November 19, 1969, Thomas Bevan wrote members of the Penphil Investment Committee:

. . . It is Ben's thought to acquire 10,000 shares of the Riveria Bank, if possible, and to realize $10 per share in an arbitrage, upon the exchange of shares for the holding company [stock].

Fleming denied any knowledge of this proposed transaction, but added that Penphil did not purchase shares of Riviera Beach. He seemed disturbed that such a proposal had been made to Penphil, saying, "Why, that would have amounted to the purchase of more than 10 percent of the outstanding shares of Riviera." At the time, there were 99,000 shares outstanding.

First Bancshares of Florida, Inc. became a registered bank holding company on October 15, 1970. Penphil exchanged its holdings of stock in the two Boca Raton banks for an equal number of shares of the bank holding company's stock. Penphil's 26,048 shares of First Bancshares represent about 5 percent of the outstanding shares of the holding company.

Since Fleming played an instrumental role in Penphil's Florida bank stock holdings, it should be noted that his banking career went beyond the activities so far described in this section of the report. Fleming told staff investigators that Comer J. Kimball, then Chairman of the Board of First National Bank of Miami, Florida's largest commercial bank, invited him to become a senior officer in that institution in 1966. He said he accepted and was elected Vice Chairman of the Board with instructions from Kimball to develop and help execute methods by which First National of Miami would increase its assets from about $500 million to $1 billion. He said his three-year stay at the bank was burdened by what he described as a frustrating relationship with Harry Hood Bassett, who was President of the institution at the time Fleming joined the bank, and who became Chairman of the Board shortly thereafter. Fleming asserted his decisions were continuously overruled by Bassett. He said he finally gave up and returned to full-time work at First Bank and Trust and University National at Boca Raton in 1969. Fleming had remained Chairman of the Board of both of these banks during his time with First National of Miami.

A somewhat different version was given by Louis J. Hector, General Counsel for First National Bank of Miami and Chairman of the Executive Committee of Southeast Bancorporation, Inc., the registered bank holding company with which First National is affiliated. Hector said that Fleming was viewed by Kimball and other members of First National's board as a dynamic, imaginative and rising figure in the Florida banking industry. Hector said Fleming was made President of Southeast Bancorporation in addition to being elected Vice Chairman of First National's board, but later was made Vice President of the holding company because he lacked the talent and perseverance necessary to make the daily wade through vital corporate details. Hector said Fleming was "used" in the State Capital, Tallahassee. Eventually, Hector said, Fleming began to spend increasing amounts of time on business connected with his Boca Raton banks, highlighted by efforts to create First Bancshares of Florida. During this period Southeast Bancorporation was also formed and, Hector said, it became apparent that the two holding companies would probably be in competition with each other. Hector said Fleming was asked in 1969 not to stand for reelection to the positions held in First National and Southeast Bancorporation.

The information cited above makes clear Penphil's interest in achieving substantial investments in a number of Florida banks by acting on advice supplied by Sawin and Fleming. Moreover, Sawin and Fleming were clearly at Penphil's service by virtue of the fact that Sawin's way into the First Bank and Trust and University National Bank was provided by Penphil and Fleming's obvious awe of the Penphil leadership, coupled with expressed delight at being allowed to purchase shares in the company. In addition, it cannot be ignored that Penphil's bank holdings put it in a position to tap large new financial resources necessary to carry out David Bevan's plans to turn Penphil into a substantial holding and operating conglomerate detailed later in this report.

Penphil's investments in the Boca Raton banks and its subsequent exchange of this stock for shares in First Bancshares of Florida, a dominant force in commercial banking in the area, takes on far more meaning when the following is recognized:

1. Boca Raton is the location of large real estate development programs being conducted by the Arvida Corporation, which is 58 percent owned by the Penn Central.
2. Arvida's board of directors is controlled by Penn Central officers. David Bevan and Charles Hodge were among the Penn Central representatives on the Arvida board.
3. The president and vice president of Arvida are Penphil shareholders.
4. David Bevan and Hodge controlled the investment programs of both Penphil and Penn Central.

All of these elements add up to a situation in which David Bevan and Hodge had maneuvered Penphil into a position to take advantage of the opportunity to profit from Arvida's real estate activities in the fastest growing area of Florida.

Penn Central's investment in Arvida is detailed in the following section of the report.

INTERLOCKING RELATIONSHIPS WITH ARVIDA

Excerpt from the July 20, 1965, meeting of the Executive Committee of the Pennsylvania Railroad Company's Board of Directors:

> The Chairman of the Finance Committee [David Bevan] reported that studies have been made of the current position and future prospects of the Arvida Corporation, a real estate development firm owning about 100,000 acres of land on both the east and west coasts of Florida, in the Miami-Fort Lauderdale-Palm Beach areas and adjacent to Sarasota. The land was acquired beginning in 1947 by the late Arthur Vining Davis and sold to the Arvida Corporation after its formation in 1958. Arvida's principal activity is selling and developing these properties, which are presently being managed by Stockton, Whatley, Davin and Company, a prominent Florida real estate management company.
>
> Among Arvida's properties are 25,000 acres now leased to Aerojet-General Corporation, sole contractor for solid fuel rockets, the Boca Raton Hotel and extensive oceanfront property at Boca Raton. Based on a price of $6 a share, the outstanding stock of Arvida represents a value of approximately $36,000,000, with estimates of the net worth per share, depending upon how the real estate is valued, ranging up to $14 and $15. Earnings for the fiscal year ending July 21, 1965, are estimated at $500,000.
>
> The Chairman of the Finance Committee stated that as a further step in the diversification program, it is proposed that a controlling interest in Arvida Corporation be acquired through the purchase, principally from the estate of Arthur Vining Davis, of 3,400,000 shares [approximately 55%] of such stock at $6 a share, or approximately $20,400,000, payment therefore to be made in three annual installments;

and that Stockton, Whatley, Davin and Company [SWD], which will continue to manage the properties at the present fee of $150,000 a year, would be granted the right to purchase, over a five-year period, approximately 35% of the number of shares purchased by this company directly or indirectly from the estate of Arthur Vining Davis. He stated that the Stockton company has agreed not to purchase additional shares of Arvida on the open market and that this company may purchase such additional shares as it deems desirable. He stated further that it is desired to sell to Pennsylvania Comapny [the Railroad's wholly-owned subsidiary] the stock of Arvida to be acquired.

The minutes disclose that after discussion, which was not detailed in the minutes, authorization by the Pennsylvania Railroad Co. for purchase of the Arvida stock was given. One-third of the total cost was to be paid at settlement, one-third one year later, and the remaining one-third two years later.

Authorization was also given for the sale to SWD of up to 10 percent of the Arvida stock held by the Pennsylvania Company, plus an option to purchase an additional amount of stock equal to 25 percent of the holdings of the Pennsylvania Company over the next five years at $6 a share plus a carrying charge amounting to 6 percent for the first option year and an additional 6 percent for each option year thereafter.

The result of the transaction is described in a report filed by Arvida with SEC, dated August 10, 1965. That report states in part:

* * * On July 26, 1965, the Pennsylvania Railroad Company purchased 3,274,428 shares of Arvida Corporation Class A common stock from the estate of Arthur Vining Davis. Immediately thereafter the Pennsylvania Railroad Company sold 222,351 of these shares to Stockton, Whatley, Davin & Company and retained 3,052,077 shares, representing 51 percent of the total outstanding stock of Arvida Corporation. Both sales were made at a price of $6.00 per share. Stockton, Whatley, Davin & Company, a wholly-owned subsidiary of General American Oil Company of Texas, also received an option from the Pennsylvania Company for the purchase of an additional 923,698 shares at a price of $6.00 per share plus certain specified carrying charges. The option was exercisable in annual installments over a five-year period and was cumulative. * * *

Brown Whatley told staff investigators that David Bevan urged Stockton, Whatley, Davin and Company not to exercise its option to purchase the additional 923,698 shares of Arvida stock during the initial years the option was in effect. Mr. Bevan's rationale, according to Mr. Whatley, was that exercise of the option would reduce Penn Central's holdings in Arvida to less than 50 percent and, if this occurred, Penn Central could no longer include Arvida in its consolidated income reports. It is hard to understand Mr. Bevan's concern over including Arvida in the Penn Central's consolidated reporting procedures, since Arvida's annual net income—which has averaged only about $500,000 a year—is completely insignificant when considered within the total Penn Central corporate picture.

Whatley told staff investigators that it was his understanding that the Pennsylvania Company had planned to ultimately own at least 80 percent of the outstanding shares of Arvida in order to achieve tax advantages that could be obtained when the investment reached this level. He said Penn Central apparently failed to do this because of the depletion of its cash resources and because its stock was not attractive enough to be accepted in an exchange offer by the minority stockholders of Arvida.

Whatley said that because of Arvida's uncertain future following the collapse of the Penn Central Transportation Company, SWD asked for and received a 90-day extension on its option to purchase additional Arvida stock when the option agreement was due to expire in July of 1970. When the expiration date of the extended option agreement approached in October, SWD asked for another 90-day extension, but the Penn Central refused and the option was withdrawn. During the 90-day extended option period, SWD negotiated a new management contract with Arvida, raising its annual fee from $150,000 to $240,000.

The purchase of 222,351 shares of Arvida stock by SWD in 1965 made it the second largest Arvida stockholder. Brown Whatley told staff investigators that SWD had notified Arvida that it did not intend to continue to provide management services for Arvida after 1964 because it was not being paid enough under its $150,000 a year plus expenses contract. Whatley said that Penn Central, which began negotiating for purchase of Arvida stock in 1964, would not make the investment unless SWD, which is one of the largest mortgage bankers in the southeast, continued to manage the real estate development company. It should be pointed out that Whatley and Davin owned 24 percent and 38 percent, respectively, of the outstanding stock of General American Oil, which owns 100 percent of SWD.

The August 10, 1965, Arvida report to the SEC notes that following the Penn Central takeover all outstanding shares of Arvida Class B common stock were converted into an equal number of shares of Class A common stock, and that the twelve-member Arvida Board of Directors was increased to fifteen by the election of three new Board members.

The three new Board members were David Bevan, Stuart Saunders and Charles Hodge. William Gerstnecker was elected to the Arvida Board in September of 1965, and Angus G. Wynne, Jr., Chairman of the Board and President of Great Southwest Corporation (which was controlled by Penn Central), was named to the Arvida Board in December of 1965. Brown Whatley and Joseph Davin of SWD and W. E. Dunwody, Jr., a partner in the law firm of Mershon, Sawyer, Johnston, Dunwody & Cole, the General Counsel for Arvida, were already on the Arvida Board. Moreover, Bevan, Saunders, Hodge and Whatley were made members of the Arvida Executive Committee.

Not only did Penn Central control the Arvida Board, but six of the 15-member Board were Penphil shareholders. Since David Bevan and Charles Hodge controlled the investment programs of both Penn Central and Penphil, and since Whatley considered Bevan to be his "boss," Penphil was in a position to control the real estate activities of Arvida.

Whatley told staff investigators that despite the fact he had invested $25,000 in Penphil, he did not make any effort to familiarize himself with Penphil's holdings. He stated that his only purpose in joining Penphil was to "cement relationships with the Railroad."

The Penn Central purchase of a controlling interest in Arvida was preceded by the purchase of condominium apartments from Arvida by David Bevan and Hodge. Located at Arvida's Sabal Point development at Boca Raton, apartment 404, which was purchased by Bevan, was priced at $46,750 and apartment 504, which was bought by Hodge, was priced at $47,250. Correspondence regarding these transactions which was submitted to the staff by Arvida indicates that Bevan paid for his apartment in full with the proceeds of a loan from the Chemical Bank. The warranty deed is dated June 23, 1965. Hodge financed slightly less than half the cost of his apartment with a mortgage issued by Aetna Life Insurance Company in the amount of $22,000 for 20 years at 6 percent interest. The closing for this transaction is dated July 12, 1965. About a year later, Hodge requested written affirmation from Arvida that he did not receive a price break on his apartment by virtue of his position on the Arvida Board of Directors and his connection with the Pennsylvania Railroad Company. On May 2, 1966, Brown L. Whatley, President of Arvida, wrote Hodge:

> Frank Steffens has written you in compliance with your request for some file evidence that you received no special treatment of any kind in connection with your purchase of your condominium unit in Sabal Point Apartments. Nevertheless, I wanted to supplement his letter with a statement of my own.
>
> Like everyone else who purchased one of our apartments at Sabal Point, you paid the full price. We have made no price concession, reduction or rebates to any of our apartment purchasers.
>
> The sale to you was handled in the normal way with the sales personnel at the office in the Sabal Point model apartment building, next door to the apartment building itself. No favors, special consideration, changes or adjustments in price or terms were asked for or granted. Our staff people and our records will substantiate these statements.

At the bottom of the letter there is a notation, "Same letter to Bevan."

Another member of Penphil known to have purchased Arvida real estate is Harry F. Ortlip, a Philadelphia electrical contractor and real estate dealer. Ortlip purchased 1½ lots at the Arvida-owned Royal Palm Yacht and Country Club in Palm Beach County. Documents regarding this case show the satisfaction of an $8,000 mortgage dated September 1, 1959, carrying interest of 6 percent and due January 1, 1961. In addition to the $8,000 sum, Ortlip paid $29,134 in cash for the property, bringing the total cost to $37,134. Immediately after purchase, Ortlip commissioned the construction of a home on the property.

Frank M. Steffens, Arvida's Senior Vice President for administration and finance, gave the following description of the financial arrangements made by Arvida to obtain the funds it needed to operate. Construction loans were obtained from the First National Bank of Miami, Florida National Bank and Trust Company of Miami, Palmer First National Bank and Trust Company at Sarasota, Chemical Bank New York Trust Company, First National City Bank of New York, Chase Manhattan Bank, and First National Bank of Boston. Comer Kimball, former Chairman of the Board of First National Bank of Miami, was also a former president of Arvida. Steffens said he thinks that David Bevan and Gerstnecker played a role in introducing Arvida to Chemical, First National City and Chase Manhattan by virtue of the fact that the Penn Central had major accounts with all these banks. Whatley established the contacts with the First National Bank of Boston, Steffens said.

Arvida's method of developing real estate can be described as follows.

After construction is completed and the property is ready for sale, a blanket mortgage on the buildings and sites is obtained from Aetna Life Insurance Company. Arvida's annual report for 1969 shows that it owed Aetna $23,325,000 at 6½ percent and that Aetna had committed itself to advance an additional $7,000,000 and to extend the payment terms of the loan from 17 to 25 years under an overall interest rate of 7.3 percent. Aetna had also been granted a right to participate in the earnings of an Arvida operating facility and had been given option to purchase designated acreage at its current market value.

In addition to these financial relationships, Arvida also maintained deposit accounts for its Boca Raton Hotel and Club in the First Bank and Trust Company of Boca Raton and the Boca Raton National Bank. The circumstances regarding the establishment of these accounts and what changes occurred thereafter are described in a letter from Steffens to David Bevan, dated May 11, 1970. It reads as follows:

> The operating bank account for the Boca Raton Hotel and Club was originally established at the Boca Raton National Bank by former management officials of Arvida Corporation, who were also the organizers, major stockholders and management of the Boca Raton National Bank. [Milton N. Weir, Sr. is president and chairman of the board of Boca Raton National. He is a former president of Arvida.] These officers discontinued their association with the Arvida Corporation in 1961.
>
> The operating bank account for the Boca Raton Hotel and Club was transferred to the First Bank and Trust Company of Boca Raton from the Boca Raton National Bank on December 15, 1966. This was accomplished by opening a new account at the First Bank and Trust Company with a $20,000 deposit. The hotel accounting department then commenced to draw operating disbursements against this account.
>
> The Board of Directors of Arvida Corporation, on July 29, 1966, formally approved and passed a resolution to open a new account at the First Bank and Trust Company of Boca Raton, and the Executive Committee, on October 21, 1966, approved the transfer of the hotel operating account to this new account.

The Executive Committee included Bevan and Hodge, who had put their stamp of approval on Penphil's purchase of First Bank and Trust Company stock during the previous month.

Returning to the letter:

> The following table of annual debits summarized the volume of business and activity in these bank accounts for the past five years.

	First Bank & Trust Co. hotel account	Boca Raton National Bank hotel account	Boca Raton National Bank regular account
1969	$10, 329, 700		$1, 952, 023
1968	7, 296, 462		266, 370
1967	6, 499, 167		675, 458
1966	97, 887	$6, 926, 286	253, 375
1965		6, 096, 057	1, 036, 096

> There are no service charges of any kind for these accounts.
>
> In 1966 the company was in the process of negotiating several very important property acquisitions which involved, directly and indirectly, Mr. Thomas J. Fleming and his wife's family. Mr. Fleming, Chairman of the Board of the First Bank and Trust Company of Boca Raton, was

at that time and is today, a prominent banker and influential local citizen. At that time, he was also serving as Vice Chairman of the Board of the First National Bank of Miami, the largest bank in the state of Florida and with whom Arvida Corporation conducted a considerable amount of its banking business.

In 1966 Arvida (through a subsidiary company) granted to the IBM Corporation a confidential option to purchase a large tract of land west of Boca Raton as the site of a manufacturing plant and research facility. Prior to IBM exercising this option, Arvida Corporation actively engaged in negotiations with several property owners in the area, including Tom Fleming and his wife's family, to obtain options to acquire additional holdings which it was felt would increase in value when IBM exercised its option and their presence in the community became public knowledge.

During the negotiations, Mr. Fleming mentioned several times his desire for his bank to handle more banking business with Arvida Corporation, especially with the Boca Raton Hotel & Club. It was apparent at that time that Mr. Fleming and his wife's family would hold substantial purchase money mortgages from Arvida Corporation arising from the purchase of the properties under option. These mortgages would be subject to continual modification in the future as to release provisions and release prices, subordinations for rights-of-way, and joinder in plats as development progressed.

The schedule of dates of both the IBM/Arvida option and the Arvida/Fleming option indicate the interrelationship of these transactions:

	IBM-Arvida	Arvida-Fleming
Letter of proposal	Apr. 8, 1966	May 19, 1966
Date of option agreement	Apr. 26, 1966	Sept. 29, 1966
Date of closing	Nov. 30, 1966	Jan. 3, 1967

The length of time elapsed between the date of the IBM/Arvida option agreement (April 26, 1966) and the Arvida/Fleming option agreement (Sept. 29, 1966) indicates the difficulty of the latter negotiations.

It was of vital importance, not only to gain the cooperation of the sellers to acquire the options prior to disclosure of the IBM purchase but also to continue this cooperation with them as mortgagees during the development phase which would require continual concessions on their part. This property which was eventually acquired by exercise of these options is now the site of Arvida Corporation's multi-million dollar Boca Raton West development.

In the 1966 discussions relating to the possible opening of a new account with the First Bank and Trust Company of Boca Raton, Mr. Fleming indicated that his bank would make available a substantial line of credit to the company. This arrangement eventually culminated in a $1,000,000 open line of credit to the company which has been used to fund the hotel inventories, receivables and other operating costs during its opening period each year. This line of credit has been important in financing the holtel's working capital, especially after the recently completed expansion program. This line also was our first line of credit from a Boca Raton bank as we had not borrowed or had a line with the other bank.[2]

Mr. Fleming's position in the Boca Raton community and as a prominent Florida banker, the need for continual cooperation on the part of him and his wife's family, and the availability of an open line of credit at his bank were the reasons for my recommendation to the Board of Directors and the Executive Committee that the hotel operating account be transferred to the First Bank and Trust Company of Boca Raton.

[2] Steffens told staff investigators that later, upon his request, he was elected to the Board of Directors of the Boca Raton National Bank, which extended a $500,000 line of credit to Arvida in return for continuation of Arvida's deposit account with the bank.

Steffens said the land in question, 1,423 acres owned by the Fleming and the Butts families (the former Miss Butts is Fleming's wife), was purchased by Arvida for a total cost of $3.3 million under a purchase money mortgage agreement providing "very good terms—a 6 percent note maturing in 1982." The agreement, he said, allowed Arvida to close the deal without having to resort to bank borrowing. Following the collapse of the Penn Central, Fleming said he placed a vendor's lien against the property for protection in the event that Arvida is unable to meet the note. The lien was later removed.

As indicated above, the original agreement under which the Penn Central through its wholly-owned subsidiary the Pennsylvania Company, was to have purchased controlling interest in Arvida called for the final payment to be made in July of 1967. Unwilling to come up with the necessary cash to do this, Pennsylvania Company's Executive Committee, at its August 28, 1967, meeting, ratified an agreement whereby final payment would be postponed for another two years.

It is interesting to note that at this same Pennsylvania Company Executive Committee meeting, a dividend of $6 million was declared out of profits for the third quarter of 1967 for common stockholders of record at the close of business on September 8, 1967, and that an extra dividend of $1,500,000 was declared out of profits for common stockholders of record as of the close of business September 29, 1967. All of the common stock of the Pennsylvania Company was and is owned by the Penn Central Transportation Company.

Louis Hector of the First National Bank of Miami, which handled the Davis estate trust account, said that the trustees of the estate initially refused to grant an extension of time to the Pennsylvania Company for final payment. During the course of negotiations, he said, it was agreed that some cash would be paid, some notes would be extended, and $3 million, which was the remaining balance, would be borrowed at the prime rate from the bank. Minutes of the Pennsylvania Company's Executive Committee disclose that the bank loan was to be paid in a series of installments, the last payment to be made on January 27, 1969. Hector said the Pennsylvania Company failed to meet this deadline and that final pyament was delayed until late 1969.

Loan records of First National Bank of Miami show that $200,000 of the $3 million loan was provided by the First Bank and Trust Company of Boca Raton and $50,000 was provided by the University National Bank of Boca Raton. It should be noted that Thomas Fleming was Vice Chairman of the Board of Directors of First National Bank of Miami, Chairman of the Board of both First Bank and Trust and University National, and a Penphil shareholder at this time.

Fleming also figured in the Pennsylvania Company's successful effort to have the $3 million note extended from January 27, 1969, to December 31, 1969. A memorandum to the files of First National Bank of Miami, dated January 20, 1969, states:

> Mr. David Bevan approached Mr. Bassett through Mr. Fleming regarding our willingness to extend the company's $3 million note . . . until December 31, 1969. . . .

Hector said the only other transaction conducted by First National of Miami with the Penn Central was to provide the Penn Central with a $2 million line of credit to back up its commercial paper. He said the

Penn Central requested and received a $1 million drawdown on the line in the spring of 1970, prior to its filing for reorganization. The only reason the line of credit was extended to the Penn Central, Hector said, was because Arvida, which was routinely borrowing from the bank, was controlled by the Penn Central. The $1 million is still owed the bank.

As noted in Part I of this report, Arvida has never paid a cash dividend on its stock. Consequently, the Penn Central has never received any return on its Arvida investment except in terms of appreciated value of the shares it holds. Steffens told staff investigators, "The only thing the Pennsylvania Company ever got from us was a $500,000 loan which has been repaid."

The Penn Central Transportation Company accounting office said the loan was made by Arvida to the Pennsylvania Company on August 23, 1967, for a 60-day period at the existing prime rate of 5½ percent. The entire amount of the loan was advanced to the Penn Central Transportation Company by its wholly-owned subsidiary, the Pennsylvania Company. The accounting office said the funds apparently were used for working capital.

On October 23, 1967, the Pennsylvania Company repaid $250,000 of the loan and the remaining balance was finally repaid July 22, 1968, after a series of extensions.

Steffens said the loanwas made on a routine basis as part of Arvida's regular efforts to make short-term investments with excess cash. "The Pennsylvania Company's paper was considered a good investment at the time", Steffen said.

Aside from benefits to Penphil, made possible through interlocking relationships with the First Bank and Trust Company and University National Bank of Boca Raton and the Arvida Corporation, there appears to be no valid reason for the Penn Central's heavy investment in Arvida. Financial and investment experts consulted by staff investigators were unanimous in their agreement that investments in real estate development companies were the last thing the Penn Central or its subsidiaries should have undertaken if the Railroad was depending on the cash return from such investments to help sustain it, as various Penn Central officials have claimed. Real estate development companies require constant and consistently large sums of money for their own investment and development purposes, and cannot afford to pay out large sums of cash to their benefactors.

HOLIDAY INTERNATIONAL TOURS

Part II of the staff report—*Case Study of a Penn Central Subsidiary: Executive Jet Aviation*—describes the creation and operation of Executive Jet Aviation (EJA,) a jet plane charter service headquartered in Columbus, Ohio. Founded in 1965, EJA was controlled and financed by the Penn Central. Loans totaling $21 million were made to EJA through the American Contract Company, a wholly-owned Penn Central subsidiary, and loans totaling $18 milllion were made to EJA on Penn Central credit by commercial banks with which the Penn Central maintained deposit and loan accounts.

In 1968, EJA acquired control of International Air Bahama (IAB), a supplementary airline flying between Nassau and Luxemburg. EJA leased to IAB a 707 jet airliner and provided complete flight crews for the craft. Staff investigators found that the EJA–IAB operation was part of an effort being made by David Bevan, Hodge, and Lassiter to establish a worldwide air passenger and freight service, backed by the financial resources of the Penn Central in violation of Civil Aeronautics Board regulations.

Early in 1968, the same year EJA moved to acquire IAB, Penphil purchased a 51 percent controlling interest in and provided all of the initial operating capital necessary for the establishment and operation of a wholesale travel agency, Holiday International Tours (HIT), located in Miami. Penphil purchased 51 percent of HIT's stock for $25,500 and made a commitment to provide the travel agency with a $200,000 line of credit, $40,000 of which has been utilized. HIT's primary purpose was to serve as general sales agent for IAB passenger tickets. In effect, the arrangement gave control of IAB passenger sales to Penphil, which was controlled by the same men who controlled EJA–IAB through the Penn Central namely David Bevan and Charles Hodge. The success of EJA–IAB would have meant automatic success for Holiday International Tours and a handsome return on Penphil's investment in the travel agency.

TURNING PENPHIL INTO A CONGLOMERATE

David Bevan's dream to turn Penphil into more than "a private investment club" is detailed in a letter, dated July 31, 1967, sent to Charles Hodge. In his letter, Bevan states:

> . . . We are thinking of having a large number of shares of Penphil outstanding and going, you might say, public ultimately with Penphil and turn it at the same time into an aggressive acquirer of other companies so that we can build it up into a very substantial conglomerate holding and operating company.

When asked about his brother's proposal for the investment club, Thomas Bevan said, "That's the way Dave thought. As chief financial officer of the railroad he was dealing with a big picture and it was just natural that he would do that with Penphil too." To a question about what happened to David Bevan's "dreams" for Penphil, Thomas Bevan said that, "Dave's eyes were bigger than his stomach. He just didn't have the time needed to expand the scope of Penphil."

The complete letter sent by David Bevan to Charles Hodge follows:

> The following letter is just for your information and to give you some idea as to the current thinking of some of us and no specific action is requested until we get along a little further.
>
> 1—If the outside holders of Florphil agree, we plan to merge Florphil into Penphil. This is both to simplify the situation and also broaden the equity bases of Penphil.
>
> 2—At the present time I am advised by my brother, Tom, that we are an exempt investment holding company. We are exempt on the basis of a limited number of stockholders. Since some of the moves we plan to make will greatly increase the number of stockholders of Penphil, we will lose this exemption. We do not desire to become a regulated investment holding company for a number of reasons. To prevent this, Tom also advises us to acquire some small company and merge it into Penphil to make Penphil an operating company. It so happens that we may be in a position to acquire a small debt free industrial company which is operating on a profitable basis and merge this into Penphil and, if so, this will be the next step after merging Florphil into Penphil.
>
> 3—There appears to be an excellent opportunity for us possibly to acquire a small mutual fund and if we are able to do this, we will hold it as a subsidiary of Penphil giving out Penphil stock in exchange.

From the foregoing you can see this will gradually broaden the equity base of Penphil if we are successful and substantially increase the number of shares outstanding. If we follow this program we will eliminate all limitations on the right of sale of Penphil stock, and actually we are thinking in terms of having a large number of shares of Penphil outstanding and going, you might say, public ultimately with Penphil and turn it at the same time into an aggressive acquirer of other companies so that we can build it up into a very substantial conglomerate holding and operating company.

If you have any questions or comments, we would be very happy to have them. Each individual move, of course, will be submitted for specific approval.

The "Florphil" referred to in the letter was a Delaware corporation formed by Penphil in January, 1967, primarily for the purpose of investing in Florida property. It existed for little more than one year. During that time it purchased 8,250 shares of common stock of the First Bank and Trust Company of Boca Raton at a cost of $214,500 and 1,700 shares of common stock of the University Bank of Boca Raton for $35,000. (Penphil's investments in these two banks were treated in greater detail previously in this report.)

A report from Haskins and Sells, CPA, November 30, 1967, placed the total market value of the bank shares at $380,750—a paper profit of 65 percent in 12 months. These were the only investments made by Florphil during its history.

Penphil owned 83.75 percent of Florphil and the balance was held by Lassiter, Manero, Ortlip, Whatley and Davin. These five persons are the "outside holders of Florphil" referred to in Bevan's letter to Charles Hodge.

On February 19, 1968, Florphil was merged into Penphil and Penphil issued 1,307 shares of stock to the five "outside holders" in exchange for the Florphil stock they held. As a result of this transaction, the five "outsiders" became members of Penphil.

In discussing Florphil with staff investigators, Thomas Bevan said that Florphil was formed to give Lassiter, Manero, Ortlip, Whatley, and Davin an opportunity to ally themselves with Penphil's investment program without having to purchase shares of Penphil stock in amounts equaling the stockholdings of the original Penphil members. The requirement that all members of Penphil must hold an equal number of shares was made part of the Penphil by-laws. The requirement, however, was changed by the merger of Penphil and Florphil, with Penphil being the surviving corporation. With the exception of Whatley, the Penphil holdings of the former Florphil members never exceeded 600 shares each. Whatley holds 1,323 shares of Penphil stock.

Further evidence of the effort to greatly expand Penphil into a major conglomerate is given in an undated, unsigned memorandum distributed to Penphil shareholders. The memorandum, which was obtained from the files of Charles Hodge, reads as follows:

PROPOSAL RE KANEB, TROPICAL AND PENPHIL

Steps to be taken—

1. Create a new holding company to be called National Industries for purposes of this memorandum.

2. National Industries will offer shares of its stock in exchange for those of Tropical and Kaneb based on their respective markets unless analyses dictate that some other basis should be used. For example, if you assume that Tropical is selling at 20 and Kaneb at 15 you might issue one share of National Industries for each share of Tropical and ¾ of a share of National Industries for each share of Kaneb.

3. Penphil would transfer its shares of Continental Mortgage to Florphil in return for a proper number of shares of Florphil; i.e., this would be based on the liquidating value of Florphil shares vs. current market for Continental Mortgage.

4. Penphil would also sell requisite number of shares of National Industries to pay off bank loans and then would liquidate the company with the net result that each present owner of Penphil would get shares of Florphil plus shares in the new holding company.

The difficulty with the above is that we lose part of the leverage and there is probably capital gains tax involved. Against this the following method might be better:

1. Create a new holding company to be called National Industries for purposes of this memorandum.

2. National Industries will offer shares of its stock in exchange for those of Tropical and Kaneb based on their respective markets unless analyses dictate that some other basis should be used. For example, if you assume that Tropical is selling at 20 and Kaneb at 15 you might issue one share of National Industries for each share of Tropical and ¾ of a share of National Industries for each share of Kaneb.

3. Penphil would transfer its shares of Continental Mortgage to Florphil in return for a proper number of shares of Florphil; i.e., this would be based on the liquidating value of Florphil shares vs. current market for Continental Mortgage.

4. Spin off Florphil to present stockholders of Penphil.

5. National Industries offer its shares in exchange for shares of Penphil as indicated by respective liquidating values.

6. Merge Penphil into National Industries.

On this basis Penphil stockholders would end up with shares of Florphil and a substantial number of shares of National Industries. Leverage would be maintained since National Industries would assume the outstanding debt of Penphil in the process of merging Penphil into National Industries. It does not seem as if there would be any tax liability involved in any of the foregoing under this plan.

It should be noted that both David Bevan's letter and the memorandum stress the point of retaining as much control as possible for the existing stockholders of Penphil while greatly expanding its scope and power. It also should be born in mind that the existence of and the ability of Penphil to expand was due almost entirely to Penphil interlocking relationships with the Penn Central and its subsidiaries, both railroad and non-railroad.

DECISION TO KEEP PENPHIL GOING

On August 20, 1970, seventy-nine days after the Penn Central Transportation filed for reorganization, Penphil stockholders held a special meeting in Philadelphia and voted to liquidate the investment club. Only three of the 26 Penphil shareholders were present—Thomas Bevan, Warren Bodman, and Francis Cannon. Together they owned a total of 9,900 shares. Their votes, together with 49,160 proxy votes out of a total of 69,238 outstanding shares, were cast to liquidate Penphil. Bodman, Cannon, Gerstnecker and Thomas Bevan were elected to form a special committee for liquidation to be completed within 12 months of the date of the meeting.

When questioned by staff investigators, Thomas Bevan said the reason for liquidation was the relative inactivity of the company in terms of acquiring new investments. The most recent investment was the purchase of stock rights in the First Bank and Trust Company of Boca Raton, Florida, in 1968.

It was the August 20, 1970, meeting of Penphil stockholders that M. A. Chamberlain of Chemical Bank referred to when he said it was his understanding that Penphil stockholders had voted to liquidate the company. Chamberlain said that the bank had neither suggested nor asked Penphil to liquidate nor had the bank ever specifically asked Penphil to make payments on the interest or principal of its loan.

But 46 days later, on October 5, 1970, things had begun to change in Penphil. On that date a special meeting of Penphil's Board of Directors was held in Philadelphia. The minutes of that meeting state in part:

> It was indicated that in light of the misleading publicity that the company had received, it would be for the best interest of the company if it were not liquidated at this time and that a recommendation rescinding the action taken at the shareholders meeting be mailed to the shareholders together with the appropriate proxy.

The "unfavorable publicity" referred to consisted of press reports disclosing the interlocking relationships that existed among many of the Penphil stockholders and Penn Central, and the common investments made by both, a situation which gave rise to suggestions of insider trading and conflict of interest. Thomas Bevan denied the existence of either situation to staff investigators. He said that he was unaware that most of Penphil's investments were held in common with the Penn Central and that in fact he knew very little about Penphil's investments. He described himself as a lawyer who had no interest in the investment field and that his main if not only function in Penphil was confined almost completely to keeping the books and arranging for loans with Chemical and payments on those loans.

The minutes of the October 5, 1970, meeting of the Penphil Board also state that:

> Due to the fact that the Bank [Chemical] had expressed a desire for payment in reduction of the loan, the sale of the stock of National Homes and U.S. Freight pledged as security for the loan was authorized.

Penphil records show that $82,407 was deposited to the Penphil account in Chemical on October 28, 1970, following the sale of National Home stock, and $198,339 was deposited in the Penphil's account in Chemical Bank on October 8, 1970, after the sale of the U.S. Freight stock. The decision to continue the operation of Penphil the following December has apparently left some of the company's shareholders with a less than satisfied attitude toward Chemical Bank over the sale of the two stocks. John May, a member of Thomas Bevan's law firm who is representing his colleague in Penphil matters, said that the investment club may end its relations with Chemical and seek credit elsewhere. He added that he did not know what other financial institution would be a likely prospect.

The special meeting of Penphil stockholders to decide the future of the company was held in Philadelphia on December 9, 1970. May said eight or ten shareholders were present and all the remaining shareholders voted their stock by proxy. The upshot of the meeting was a nearly unanimous decision to rescind the resolution calling for the liquidation of Penphil and to continue the company for an indefinite period. Only one shareholder, Hodge, who voted by proxy, was reported to have been against continuation. When questioned about this, Hodge said he needed the money because of the deteriorating Wall Street situation in general and the financial problems of his investment banking firm in particular.

Both May and Thomas Bevan told staff investigators that the decision to continue Penphil was based on tax considerations, pride of shareholders who do not want to appear to be running away from the glare of public attention focused on their company, and because Penphil will become far more active in the future in terms of acquiring new investments. When questioned further on this point, May admitted that continued existence of the corporation might serve to protect individual shareholders regarding possible liability in any litigation that might be initiated by Penn Central stockholders against Penphil on charges of insider trading and conflict of interest.

Thomas Bevan tendered his resignation as President of Penphil at the December 9 meeting and was replaced by Samuel Breene. Thomas Bevan stated that he will no longer participate in the administration of Penphil, although he intends to retain his stockholdings. Asked why he had resigned, Bevan said he acted because of publicity and Penphil's need for more active direction.

Thomas Bevan has told staff investigators that so far as he is concerned, it was entirely coincidental that Penphil held common investments with the Penn Central. He stressed that there is no evidence of insider trading by virtue of the fact that Penphil, with the exception of its Great Southwest stock, held on to all its investments. He apparently excluded the sale of National Homes and U.S. Freight stock on the ground that these investments were sold under pressure from Chemical Bank to reduce Penphil's outstanding loan balance with the bank.

It was pointed out to Thomas Bevan that Penphil held its 10,000-share block of Great Southwest stock for a 17-month period during which the Penn Central controlled Great Southwest.

Bevan replied that the Great Southwest stock was sold at a paper loss considering the fact that the per share value later rose to a high point of around $430. At the same time, both he and May acknowledged that Penphil made almost a 130 percent profit when the Great Southwest stock was sold for $377,500 in December 1965.

It was then pointed out by staff investigators that Penphil could have controlled Kaneb Pipe Line and Tropical Gas by virtue of the interlocking relationships these two companies had with Penphil, Penn Central and Glore Forgan, and by virtue of common investments held by Penphil and Penn Central in the two companies. Thomas Bevan answered that there is no evidence that the opportunity for such dominance by Penphil was ever utilized. He said, "Frankly, I'm surprised to know that Penphil could have been controlling Tropical Gas."