BEFORE THE NATIONAL BUSINESS CONDUCT COMMITTEE

NASD REGULATION, INC.

In the Matter of Market Regulation Committee Complainant, vs. Kevin Eric Shaughnessy Pittsburgh, Pennsylvania, Respondent.	DECISION Complaint No. CMS950087 Market Regulation Committee Dated: May 27, 1997

This matter was appealed by respondent Kevin Eric Shaughnessy ("Shaughnessy") pursuant to Article III, Section 1 of the NASD's Code of Procedure (now Procedural Rule 9310(a)). Under review is a decision of the Market Regulation Committee ("MRC") dated June 26, 1996, which found that Shaughnessy violated Conduct Rules 2110, 2120, and 3030 by accepting monies from a stock promoter in return for recommending the purchase of certain stocks to his customers, without informing those customers or his employer brokerage firm about such payments. For the reasons discussed below, we affirm the findings of violation and modify the sanctions imposed to include a bar in all capacities from association with any member of the Association.

Background

Shaughnessy entered the securities industry in 1991 as a general securities representative. From May 1992 until April 1995, which includes the period relevant to the complaint, he was registered in the same capacity with Gruntal & Co., Inc. ("Gruntal" or "the firm"). He currently is registered with another NASD member, Meyers Pollock Robbins, Inc.

MRC Proceedings

The Complaint. The two-cause complaint was issued by the MRC on July 24, 1995. Cause one alleged the following facts: In December 1993, Shaughnessy was contacted by a non-registered

individual identified as "JJ."[1] Shaughnessy entered into an "arrangement" with Janson whereby Shaughnessy agreed to sell shares of Metallurgical Industries, Inc. ("Metallurgical" or "MTALA") common stock to Shaughnessy's retail customers in exchange for compensation equal to 15 percent of the cash value of the shares he sold. Also in December 1993, Shaughnessy sold 20,000 shares of MTALA to a customer of his firm, and he received $1,000 in compensation for the sale.[2] Shaughnessy did not disclose the MTALA arrangement or the compensation to Gruntal, or to his customer. In January 1994, Shaughnessy sold fewer than 1,000 shares of MusicSource U.S.A., Inc. ("MusicSource" or "MUSE") to four Gruntal customers,[3] and he received, again by wire from MM's account, approximately $675 in compensation for those sales. Shaughnessy did not disclose the MUSE arrangement or compensation to Gruntal or the customers. Shaughnessy's conduct was alleged to have violated Article III, Sections 1 and 18 of the Association's Rules of Fair Practice (now and hereinafter referred to as "Conduct Rules 2110 and 2120").

Cause two of the complaint alleged that Shaughnessy failed to provide prompt written notice to Gruntal that he was employed by and/or accepted compensation from a stock promoter identified as "MM,"[4] for his efforts in selling MTALA and MUSE to his retail customers, in alleged violation of Article III, Sections 1 and 43 of the Association's Rules of Fair Practice (now and hereinafter referred to as "Conduct Rules 2110 and 3030").

Answer. In answer to cause one of the complaint, Shaughnessy admitted that he had been contacted by Janson in the Summer of 1993, and that Janson offered to pay Shaughnessy an amount equal to 15 percent of the cash value of any shares of MTALA common stock he sold. Shaughnessy contended that he did not promise to sell or attempt to sell any shares of MTALA at that time. Shaughnessy also admitted that he sold 20,000 shares of MTALA to a Gruntal customer in December 1993, that he received $1,000 in compensation for that sale, and that he did not disclose the MTALA arrangement or compensation to his customer. Shaughnessy denied, however, that he failed to disclose to Gruntal the offer of Janson to pay Shaughnessy a bonus on the sale of certain shares of stock. Shaughnessy further admitted that in January 1994 he sold fewer than 1,000 shares of MUSE to Gruntal customers. Shaughnessy contended that the names of three MUSE customers were supplied to

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[1] The complaint did not specify JJ's full name. Later in the MRC proceeding, JJ was identified as "Jody Janson," and we will hereinafter refer to him as "Janson."

[2] The money was wired to Shaughnessy's account from the account of Mark McElvy ("MM"), who Shaughnessy identified as JJ's partner.

[3] Although the complaint referred to sales of MUSE to four customers, the record shows that Shaughnessy sold MUSE to only three customer accounts.

[4] The complaint did not specify MM's full name, which was stated as "Mr. McElvy" at the MRC hearing.

him by Janson; that they requested receipt of the stock certificates; and that, once they received the stock certificates, they never talked to Shaughnessy or, to his knowledge, Gruntal again. Shaughnessy also stated that one MUSE customer was his mother and that, with the exception of her, the other customers were customers of Gruntal only in the most "technical sense," since they were not Gruntal customers before or after the transaction. Shaughnessy admitted that he received approximately $675 in compensation for the MUSE sales, and that he did not disclose the MUSE arrangement or the compensation to the customers.

Shaughnessy further stated that Janson called him in the Summer of 1993, offered to provide "leads" regarding individuals who were interested in investing in securities issued by companies that Janson's firm was promoting, and stated that, from time to time, Janson's firm would pay a bonus of 10 to 15 percent on any sales of securities which it promoted. Shaughnessy asserted that he asked Janson if it was legal for him to accept such a payment, and Janson told him that he (Janson) was a former broker and "knew for a fact" that it was legal. Shaughnessy further stated that he spoke to his supervisor at Gruntal, Greg Shutok ("Shutok"), who told him to accept the leads, but not to solicit the sale of any stock priced under $3 per share because Gruntal had a policy against such sales. Shaughnessy stated that he asked Shutok about taking the money if it was offered, and Shutok said that he (Shutok) would not take the money because Gruntal also had a policy against that. According to Shaughnessy, Shutok failed to tell him that taking the money would be "illegal" or against the Association's Rules of Fair Practice, or that if Shaughnessy took the money, he would have to disclose that fact to the customer and tell Gruntal in writing. Shaughnessy's answer also asserted that Shutok's statements did not allow him to determine how seriously Gruntal took its policies, and that he had no other way to learn about problems associated with accepting payments from third parties. Shaughnessy also stated that Gruntal did not tell registered representatives about its policy or that taking money from third parties violated the Association's Rules of Fair Practice. Shaughnessy stated that the policy was not in Gruntal's manual. Moreover, Shaughnessy's answer stated that Conduct Rules 2110 and 2120 are very general and do not mention prohibitions on taking payments from third parties. Shaughnessy maintained that he had not intended to violate any interpretations of those sections, and that he took reasonable steps to comply with the rules and act in accordance with the information he was given.

In his answer to cause two of the complaint, Shaughnessy admitted that he failed to provide prompt written notice to Gruntal that he was employed by and/or had accepted compensation from MM, a stock promoter, for his efforts in selling MTALA and MUSE to his retail customers. With the exception of his mother, Shaughnessy denied that he sold shares of MUSE to people who were his retail customers, except in the most "technical sense," as the remaining MUSE customers had been supplied by Janson. Shaughnessy also denied that he knew of Conduct Rule 3030 or had any intention to violate it. Shaughnessy stated that he had a reasonable expectation that his supervisor, Shutok, would fully and completely explain to him the Association's rules with respect to the proposed payments from Janson. Shaughnessy argued that when Shutok failed to refer him to Conduct Rule 3030 or describe such a rule, he had no reason to look further and reasonably believed that he had no obligation to report any payments from Janson. Shaughnessy's answer further noted that it was not until several

months after his first contact with Janson that Shaughnessy sold any stocks promoted by Janson, for which Shaughnessy received a total of $1,675.

MRC Hearing and Decision. On February 23, 1996 an MRC hearing was held. In a decision dated June 26, 1996, the MRC made findings consistent with the allegations of the complaint and Shaughnessy was censured; fined $11,675; suspended in all capacities for six months; required to requalify by examination as a general securities representative; required to repay $250 in losses to his mother and $140 to customer "R"; required to repay customers $1,526.37 in commissions; and assessed $1,839.75 in costs.

This appeal followed.

Facts

The evidence included testimony from an Association analyst ("the Analyst"), who conducted an investigation into the trading done by Shaughnessy for his clients in MTALA and MUSE. The Analyst requested information from Shaughnessy and interviewed him both informally by telephone and on the record. The Analyst testified that in the informal telephone interview, Shaughnessy said he knew Janson from answering an advertisement for "free leads" contained in an issue of the Registered Representative magazine. The Analyst also stated that Shaughnessy initially claimed that he had received the money from Janson for selling him leads.

The Analyst also participated in an on-the-record interview of Shaughnessy, during which Shaughnessy said that his informal telephone interview statement -- that he had received the compensation for selling Janson leads -- was untrue. On the record, Shaughnessy stated that the money he had received from Janson was compensation for soliciting public customers to purchase shares of MTALA and MUSE. Shaughnessy testified that he had "prayed" and decided to tell the truth, and he claimed that Janson instructed him to tell MRC staff that the money he received was from Janson's purchase of leads. Shaughnessy also stated that, in order to support this story, Janson had provided him with a back-dated letter stating that he was paying Shaughnessy for leads. Shaughnessy also admitted in this interview that he did not disclose the compensation he was receiving from Janson to his customers, or to his firm.

At the conclusion of Shaughnessy's on-the-record interview, MRC staff informed him that they would be presenting a memorandum to the MRC requesting the authorization of a formal complaint. In response to this action, Shaughnessy submitted a document alleging mitigating facts, in which he stated that he had discussed his relationship with Janson with his manager, Shutok, who told him that Gruntal had a policy restricting the solicitation of securities priced under $3, but "[o]ther than that he [Shutok] saw no problems." This statement was not consistent with Shaughnessy's testimony in his on-the-record interview, during which he stated that he did not check with anyone concerning the legality of his relationship with Janson.

The record also included monthly bank account statements for Shaughnessy, which indicated his receipt of wire transfers in the amounts of $1,000 and $675 on December 9, 1993 and January 25, 1994, respectively. Based on order tickets and confirmations for the transactions for which Shaughnessy received compensation from Janson, a schedule prepared by the Analyst showed that Shaughnessy earned total commissions of $1,526.37 from Gruntal for the sales in MTALA and MUSE to his customers, and received undisclosed compensation from Janson in the amount of $1,675.

Additionally, the new account documentation and monthly account statements for the accounts of the four customers who purchased MTALA and MUSE from Shaughnessy showed that, contrary to statements in Shaughnessy's answer that Janson had supplied him with customer names, these accounts were opened long before the customers purchased the securities for which Shaughnessy received compensation from the promoter.

Shutok testified that he has been in the securities industry since 1969 and was Gruntal's Pittsburgh office vice president and general manager during the period relevant to this action. Part of Shutok's duties included the supervision and training of new brokers. In that regard, Shutok testified that he discussed compliance issues in meetings throughout each month, and that he met with new brokers an additional one to three times per week for their first nine to 12 months on the job.

Shutok stated that Gruntal has a compliance manual, and that Shaughnessy received a copy of that manual. Shutok noted the portion of the manual containing the policy prohibiting representatives from accepting "fees (including finder's fees), or other renumeration [sic] without the Firm's approval." Shutok testified that he had discussions with registered representatives about undisclosed compensation from promoters for selling particular securities, that he told them it was prohibited, and that he advised them that they would be terminated if they took such compensation. He also testified that he had discussed this issue, when Shaughnessy was present, on a number of occasions.[5] Shutok stated that he had heard that solicitors were calling the firm, which prompted him to call a meeting and tell those in attendance to "stay away from promoters generally." He also said that he told them that the penalty for getting involved with promoters was termination, and that such activity could jeopardize their securities licenses. Shutok agreed that he told registered representatives that they could use the customer leads given to them by promoters, as long as they discussed suitable investments with those individuals, and not stock which the promoter was promoting. Shutok denied telling Shaughnessy that taking undisclosed compensation from a promoter was only against Gruntal policy.

Shutok also testified that, after the Association already had begun its review of Shaughnessy's activities, he had a one-on-one conversation with Shaughnessy regarding the taking of undisclosed compensation from promoters for selling specific securities, Shutok said he asked Shaughnessy if he

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[5] Shutok did not recall specific dates on which Shaughnessy was present at such meetings.

(Shaughnessy) had received any compensation or "kickbacks" from anyone, and that Shaughnessy denied ever having done so.

Shaughnessy testified that, after graduating from college, his first job in the securities industry was with Hibbard Brown & Co., Inc. ("Hibbard"), for less than one year, and that he received no compliance training at Hibbard. Shaughnessy also stated that there were no questions on the issue of accepting compensation from someone other than your employer on the Series 7 or Series 63 examinations, nor was that subject addressed in any study materials that he had received.

Shaughnessy testified that he was hired at Gruntal in May 1992 by Shutok and that his initial training consisted of "product information meetings." Shaughnessy admitted that during his first few weeks at Gruntal, he received a copy of the firm's compliance manual and signed a receipt for that manual. He claimed, however, that he did not receive any training concerning the contents of the manual, the Association's Rules of Fair Practice, or what actions would constitute doing business away from a firm.

Shaughnessy testified that during the Summer of 1993, he saw an advertisement in Registered Representative magazine containing an 800 number to call for "free leads." Shaughnessy telephoned that number and spoke to Janson, who said he was a stock promoter paid to "get the story out on these young emerging companies, and [that he would] share some of that fee with [Shaughnessy] from time to time" if Shaughnessy agreed to listen to his ideas. Shaughnessy faxed his business card to Janson and received some leads from Janson a few days later. Shaughnessy testified that he understood that Janson was a stock promoter and that Shaughnessy could receive compensation from Janson for selling particular stocks.

Shaughnessy stated that he discussed his telephone conversation with Janson with Shutok, who cautioned him "very strongly," and told him that Gruntal representatives are not allowed to solicit stocks under $3 and that he would "get in trouble for it." Shaughnessy testified that he also told Shutok that Janson offered to pay him a bonus. Shaughnessy testified that Shutok told him that he could take the leads, but that he should only sell those customers stocks that were suitable. Shutok also told him that accepting a bonus from a promoter was against Gruntal's policy, and "[that he] wouldn't do it if [he] were [Shaughnessy]."

Shaughnessy testified that, after Janson faxed him the leads, Janson sent him a package of information on a company called En-Viro. Shaughnessy did not have any investors who would have been interested in this company, so he did not discuss En-Viro with any of his customers. Thereafter, Janson sent Shaughnessy information on several other companies, but Shaughnessy also did not attempt to sell securities of those companies to his customers.

In early November 1993, Shaughnessy sent Janson a prospectus, and Janson's accountant opened an account with Shaughnessy. Thereafter, Shaughnessy and Janson began speaking more

frequently. The first stock promoted by Janson which Shaughnessy discussed with a client was MTALA. According to Shaughnessy, the customer, RL, was one of his former college professors, and a sophisticated investor, who eventually bought 30,000 shares of MTALA during December 1993 and January 1994. RL sold his MTALA shares in February 1994, and realized a profit of more than 50 percent. Shaughnessy admitted that he had not wanted Gruntal to find out that he had executed trades for which he would receive undisclosed compensation, but he denied marking RL's order tickets "unsolicited" to conceal the true nature of the transactions. Shaughnessy admitted receiving $1,000 in compensation from the promoter for RL's MTALA purchases.

Thereafter, Janson called Shaughnessy to tell him about MUSE. Shaughnessy said he telephoned this company, spoke with someone in its investor relations department, and was satisfied that it was a good company. Shaughnessy sold a total of 3,000 shares of MUSE to three customer accounts, including 1,000 shares to his mother's account. One customer sold the shares for a total loss of $140. Shaughnessy's mother sold her shares at a loss of $250. The third customer left the country and took the stock with him. Shaughnessy admitted receiving $675 in compensation from Janson for the MUSE sales. Shaughnessy also acknowledged that the statement in his answer, that the customers to whom he sold MUSE were customers in name only, was incorrect, and he attributed the error to a misunderstanding by his former counsel.

Shaughnessy testified that he did not learn that his acceptance of compensation from Janson was a violation of NASD rules until the Summer of 1994, when Shutok called a meeting in which he stated that "taking a kickback of any kind was against the rules and that we would be fired if we did it." Shaughnessy said he realized at that point that he "had a problem." He telephoned Janson and asked if he could pay the money back. According to Shaughnessy, Janson responded that paying the money back would not make a difference and that what Shaughnessy did was "completely legal." Shaughnessy said he was "afraid" and did not speak to Shutok or anyone in the legal department at Gruntal about his situation, did not disclose the compensation to the firm, and "just prayed that nobody would ever find out." Shaughnessy maintained that he had had no intent to deceive, and that he never would have risked his career for $1,675 if he had known his conduct was improper.

NBCC Proceedings

An appeal hearing was conducted on December 3, 1996 before a subcommittee ("the Subcommittee") of the National Business Conduct Committee ("NBCC"). Shaughnessy, through counsel, submitted an appeal statement and participated in the hearing, as did counsel for the MRC.

Discussion

Procedural Issues. Shaughnessy's main arguments on appeal were procedural. He maintained that portions of the MRC appeal brief, and attachments thereto, should be stricken because references were made therein to documents which had not been introduced in, and were irrelevant to, this

proceeding. The documents consisted of press releases and criminal indictments of other individuals who, as argued by the MRC counsel, allegedly had engaged in conduct similar to that committed by Shaughnessy. The Subcommittee granted the motion to strike, determined to treat these new documents and references as a motion to adduce additional evidence pursuant to Procedural Rule 9312(a), and denied that motion because the information failed to meet the materiality requirement of Procedural Rule 9312(a).[6] We affirm the Subcommittee's denial of the motion to adduce additional evidence and agree with its ruling that the copies of press releases and indictments submitted did not constitute legal argument, as they represented only the beginning stages in ongoing litigation matters, and that they also were not material factual evidence, as they only indicated other prosecutors' legal theories.

Shaughnessy also argued that the complaint must be dismissed because Shutok had committed perjury in his hearing testimony before the MRC, and that the NASD had suborned (induced or procured) this perjury. Shaughnessy stated that Shutok had testified to having had a conversation with Shaughnessy in which Shaughnessy denied having received kickbacks from stock promoters. Shaughnessy argued that such testimony was contrary to an affidavit which Shutok had provided to MRC staff on November 21, 1995, in which he stated that he did not recall having any one-on-one conversations with Shaughnessy concerning receiving compensation from stock promoters for selling particular stocks to Gruntal clients. Shaughnessy contended that MRC staff knew that Shutok was not telling the truth in his affidavit, and therefore wrongly had permitted the false statements to be made.

In response, counsel for the MRC argued that staff had interviewed Shutok during its investigation of this matter, and, based on these interviews, had drafted the November 1995 affidavit for his approval and signature.[7] MRC staff stated that, three months later, when Shutok was testifying at the MRC hearing, he recalled that, after the NASD had begun its investigation in early 1995, he had a conversation with Shaughnessy about why the NASD was looking at the MTALA and MUSE trades. Shutok testified that he asked Shaughnessy at that time "if [Shaughnessy] had taken a kickback or anything from the promoter, and [Shaughnessy] denied it completely." The MRC counsel argued that he had attempted to introduce Shutok's affidavit so that Shutok could clarify the statements in the affidavit with his testimony at the MRC hearing, but that such attempts had been "thwarted" by Shaughnessy's counsel's objection to the introduction of the affidavit. In any case, the MRC counsel argued that Shaughnessy's counsel had ample opportunity to cross-examine Shutok regarding his

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[6] Procedural Rule 9312(a) provides that the party seeking to adduce new evidence has the burden of demonstrating both that there was good cause for failing to adduce the evidence at the prior proceeding and that the evidence is material to the proceeding.

[7] MRC staff noted that the affidavit had not been relied upon by the MRC and that it had not been introduced into evidence in the MRC proceeding because Shaughnessy's counsel had objected that the affidavit was irrelevant because Shutok was available to testify. In order to consider Shaughnessy's appeal arguments concerning the affidavit, the Subcommittee determined to overrule the MRC's ruling and admit the affidavit into evidence. We affirm this determination.

conversations with Shaughnessy.

We do not find any indication here of wrongdoing on the part of MRC staff. Counsel for the MRC sought to introduce the Shutok affidavit in an attempt to have the witness clarify his statements in the affidavit with his hearing testimony. Further, there is no indication in the record from Shutok that any one-on-one conversation with Shaughnessy about kickbacks had occurred before Shaughnessy accepted the payments. Shutok's testimony merely states that he asked Shaughnessy about the possibility of his having taken kickbacks "or anything" after the NASD had begun its investigation of the MTALA and MUSE trades. Accordingly, there is no corroboration for Shaughnessy's statements that he asked Shutok whether he could receive the bonuses and was told only that such action was against Gruntal policy, a statement which Shutok absolutely denied ever having made.[8]

Shaughnessy also argued that the record must be reopened because Shutok perjured himself by testifying that no notes were taken during several morning training sessions for new brokers at which he lectured that taking kickbacks from promoters for selling particular securities was "against rules, regulations, our firm policy, and they would be fired." Shaughnessy's counsel asserted that testimony from two former Gruntal brokers showed that Shutok's secretary would attend the meeting and take notes, and that he was unable to cross-examine Shutok effectively without these notes. We find that the record supports Shutok's statement that his secretary was not present at the morning training sessions for the new brokers, although she did attend and take notes at the full staff meetings held by Shutok which the brokers also were required to attend. We find that Shutok's testimony on this issue was credible, and we also find that Shaughnessy has not articulated any valid reason for reopening the hearing process to permit him to review the secretary's alleged notes.[9]

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[8] The MRC did not make a specific finding that it found Shutok's testimony in this regard more credible than that of Shaughnessy. Apart from the fact that Shaughnessy has admitted to the actions alleged in the complaint, we believe that there is sufficient evidence in the record to question Shaughnessy's credibility: 1) Shaughnessy admitted that he lied to the Analyst during the informal telephone interview when he stated that he was paid by Janson for selling leads, when in reality the payments were kickbacks; 2) Shaughnessy admitted that he intentionally told the promoter that he sold more shares of MUSE than he actually did in order to receive a larger kickback; 3) Shaughnessy marked the order tickets for the MTALA and MUSE trades as unsolicited even though he admitted that he recommended the trades to his customers; and 4) Shaughnessy signed a document that indicated that he should familiarize himself with the contents and requirements of the Gruntal manual, but he admitted that he did not read the manual.

[9] The former Gruntal brokers' testimony was not dispositive on the issue of topics discussed at compliance meetings. One witness, Brock Malky ("Malky"), who admitted that he did not attend every morning training meeting, stated that he only recalled discussions of suitability at such meetings, and stated that it was possible that there were training sessions of which he was unaware at which Shutok discussed the inappropriateness and illegality of taking kickbacks from promoters. The other witness,

After a careful review of the entire record, including the parties' arguments and briefs on appeal, we affirm the MRC's findings of violation and modify the sanctions.

Cause One. The record clearly supports the MRC's finding that from May 1992 to April 1995, while Shaughnessy was registered as a general securities representative of Gruntal, he made certain sales of MTALA and MUSE stock to customers, without informing the customers that he was receiving compensation for those sales from a stock promoter. Shaughnessy admitted that he received total compensation of $1,675 from the sales of MTALA and MUSE at issue. We concur with the MRC's conclusion that this misconduct was in violation of Conduct Rules 2110 and 2120, as alleged in cause one of the complaint.

Conduct Rule 2120, the NASD's anti-fraud rule, is the equivalent of SEC Rule 10b-5. Rule 2120 provides that no member shall effect any transaction in, or induce the purchase or sale of any security, by means of any manipulative, deceptive, or fraudulent device. In order to find violations of Rule 2120, there must be a common showing that: 1) misrepresentations and/or omissions were made in connection with the purchase or sale of securities; 2) the misrepresentations and/or omissions were material; and 3) they were made with the requisite intent, i.e., scienter.

Materiality is determined by reference to the extent to which a reasonable investor would view the fact as significantly altering the "total mix" of information about the investment. Basic, Inc. v. Levinson, 485 U.S. 224, 230-32 (1988) (quoting TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976)). In this matter, we find that the omissions were material because a reasonable investor would find it material that his or her stockbroker was receiving extra payment, from an outside stock promoter, to solicit and sell certain stock to customers. It is reasonable to infer that this fact might have altered the "total mix" of information for the MTALA and MUSE customers, who might have believed that Shaughnessy had reasons to sell those stocks other than a belief that those investments were suitable for the particular customers. See In re Gilbert A. Zwetsch, 50 S.E.C. 816 (1991) (a securities salesperson is required to disclose material adverse facts of which he or she is, or should be, aware, which includes disclosure of "adverse interests" such as "self-interest that could influence a salesman's recommendation").

We find that Shaughnessy's failure to inform the MTALA and MUSE customers that he was receiving outside compensation from stock promoters to solicit such sales was a material omission made "in connection with" the sales of securities, as Shaughnessy has admitted that he effected the transactions at issue without informing the customers of his "bonus." We find that the fact of such bonuses was

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David Mihalik ("Mihalik"), also admitted the possibility that Shutok had a meeting which he did not attend at which the receipt of kickbacks may have been discussed, and he stated that he knew that at least one other Gruntal broker had remembered such a meeting.

material information which the investors should have had prior to their purchases.

Scienter has been defined as an "intent to deceive, manipulate or defraud." Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976). Scienter also may be established by a showing that the respondent acted recklessly. See, e.g., In re DWS Securities Corp., 51 S.E.C. 814 (1993). "Recklessness" has been defined by a majority of the federal circuit courts of appeal as being "not merely simple, or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers that is either known to the defendant or is so obvious that the actor must have been aware of it." Hollinger v. Titan Capital Corp., 914 F.2d 1564, 1569 (9th Cir. 1990).

We also find that Shaughnessy possessed the requisite scienter, i.e., intent or recklessness, and that his misconduct therefore was violative of both Conduct Rules 2110 and 2120. Shaughnessy knew he received the payments from the promoter to sell shares of MTALA and MUSE to his customers, and he knew that he did not tell his customers about the payments. These circumstances are sufficient to support our finding that Shaughnessy acted willfully and/or recklessly.

Accordingly, we find that Shaughnessy's misconduct was in violation of Conduct Rules 2110 and 2120, as alleged in cause one.

Cause Two. There is no real dispute as to the facts regarding the allegation that Shaughnessy violated Conduct Rules 2110 and 3030 by failing to provide prompt written notice to Gruntal that he had accepted compensation from a stock promoter for his efforts in selling MTALA and MUSE to his retail customers. Although Shaughnessy testified that he had asked Shutok about the propriety of such payments, there is no question that Shaughnessy did not provide any written notice to Shutok, or anyone else at Gruntal, of his intent to accept the money from the promoter, or his receipt of the actual payments. Further, even if Shaughnessy's testimony about his conversation with Shutok is taken at face value, Shaughnessy admitted that Shutok informed him that such actions would be contrary to Gruntal policy, and that he [Shutok] would not engage in such conduct. Shaughnessy was thus aware that his conduct was, at the least, not totally above board, and yet he persisted with the sales of MTALA and MUSE, accepted the payments, and hid his actions from everyone at Gruntal. Shaughnessy admitted that he did not want anyone to know about the payments, and at various times he stated, inconsistently, that he did not want his colleagues to know that he could not succeed in the business without the bonus payments, and also that he understood from his conversation with Shutok that the firm had a policy against such payments, so he wanted them kept a secret.

The bottom line is that Shaughnessy never provided any formal written notice of his outside compensation to Gruntal, and in fact, did his very best to conceal his misconduct. Shaughnessy admitted that his concealment continued past the time when he acknowledges that Shutok held a meeting in the Summer of 1994 and advised Gruntal staff that they could be terminated for accepting payments from promoters. Shaughnessy stated that his silence was due to fear, and that he simply

hoped that nobody at the firm would find out. Yet, the record shows that even as late as Spring 1995, when the NASD began its investigation, Shaughnessy gave inconsistent statements to MRC staff about the source of the payments, and submitted the false back-dated letter from Janson in an attempt to assert that the payments had been for providing customer leads to Janson.

Accordingly, we find that Shaughnessy violated Conduct Rules 2110 and 3030 as alleged in cause two.

Sanctions. Upon consultation with the applicable NASD Sanction Guidelines ("Guidelines"), we affirm the censure; the $11,675 fine (consisting of a $10,000 fine ($5,000 for cause one and $5,000 for cause two) and disgorgement to the NASD of $1,675 in undisclosed compensation from the stock promoter)); the requirements that Shaughnessy repay $250 in losses to his mother and $140 in losses to customer “R”, and repay customers $1,526.37 in commissions; and the assessment of $1,839.75 in MRC costs. Due to the serious underlying misconduct at issue here, as well as Shaughnessy's attempts to conceal his actions during the MRC's investigation, we also have determined to impose on Shaughnessy a bar in all capacities from association with any member of the Association in lieu of the six-month suspension and requalification requirement imposed by the MRC.

In reaching these sanctions, we have considered Shaughnessy's argument that he never actually was informed by Shutok, or Gruntal, or Hibbard (Shaughnessy's first employer in the securities industry) that his actions would be considered a violation of the Association's rules. Shaughnessy was a Series 7 registered representative, and as such, he must be held to a standard of knowledge about the industry and a sense of his obligations to investors. In re Patricia H. Smith, Exchange Act Rel. No. 35898 (June 27, 1995). Shaughnessy's conduct in receiving kickbacks from promoters was so clearly improper that any person who possesses a Series 7 registration should recognize it as such. In addition, the record shows that Shaughnessy received a copy of the firm's compliance manual, and signed a statement that "[h]e [understood] that [he] should thoroughly familiarize [himself] with the Gruntal & Company Policy and Procedures manual and understand its contents and requirements," which included a section explaining that it was a violation "of securities laws, regulatory rules, Firm policies and/or ethical business practices" to accept "gratuities, fees (including finders' fees), or other renumeration (sic) without the Firm's approval."

We also have considered Shaughnessy's arguments that he had been advised by Shutok that accepting monies from stock promoters was only against Gruntal policy, and that he had no reason to doubt this information or seek to learn if there actually were any Association rules prohibiting such activity. Even assuming, arguendo, the truth of these factual assertions, we reject the premise that Shaughnessy's conduct would be excused by such circumstances. The Commission repeatedly has held that it is "no defense that others in the industry may have been operating in a similarly illegal or improper manner." In re Charles E. Kautz, Exchange Act Rel. No. 37072 (April 5, 1996) (citing In re Donald T. Sheldon, 51 S.E.C. 59, 66 n. 32 (1992), aff'd, 45 F.3d 1515 (11th Cir. 1995)); In re Benson & Co., Inc., 42 S.E.C. 107, 111 (1964). Further, the Commission consistently has held that "ignorance of

NASD requirements is no excuse for violative behavior." Kautz, supra at n. 11. See also, Carter v. SEC, 726 F.2d 472, 473-74 (9th Cir. 1983) (rejecting representatives' defense that they were unaware of NASD rules regarding private sales of securities, stating "[a]s employees, [the representatives] are assumed as a matter of law to have read and have knowledge of these rules and requirements"); Sirianni v. SEC, 677 F.2d 1284, 1288 (9th Cir. 1982); In re Gilbert M. Hair, 51 S.E.C. 374, 378-79 n. 12 (1993); Smith, supra.

In deciding to impose a bar on Shaughnessy, we have looked to the Guideline for material omissions which provides that where materially false statements (or omissions) were intentionally or recklessly made, as we have found here, consideration should be given to a suspension for at least three months or a bar, particularly in egregious cases.[10] In view of the particular circumstances of this action, which involve serious misconduct and attempts by Shaughnessy to thwart the Association's investigation by providing inconsistent statements and a false, back-dated, and allegedly exculpatory letter to MRC staff, we have determined that a bar in all capacities is necessary for Shaughnessy's misconduct. Further, the Commission has found that it is necessary to bar respondents who, like Shaughnessy, fail to accept responsibility for their own actions and continue to place the blame on others for the circumstances which have occurred. See In re Patrick G. Keel, 51 S.E.C. 282 (1993) (SEC concluded that Keel must be excluded from the securities business, and noted that he had not taken "responsibility for his actions but, rather, blames his supervisor and his customers for what occurred").

[10] The Guideline for outside business activities also states that when willful intent to circumvent the rule is demonstrated, a suspension of one to 30 days should be considered.

Accordingly, Shaughnessy is censured; fined $11,675; barred in all capacities from association with any member of the Association; required to repay $250 in losses to his mother and $140 to customer "R"; required to repay customers $1,526.37 in commissions;[11] and assessed $1,839.75 in MRC costs and $750 in appeal costs. The bar is effective immediately upon issuance of this decision.[12]

On Behalf of the National Business Conduct Committee,

Joan C. Conley, Corporate Secretary

[11] The commissions are set forth in a schedule identified as Complainant's Exhibit No. 21 in the MRC proceeding, at Record Page 540, which is also attached hereto.

[12] We have considered all of the arguments of the parties. They are rejected or sustained to the extent that they are inconsistent or in accord with the views expressed herein.

Pursuant to NASD Procedural Rule 8320, any member who fails to pay any fine, costs, or other monetary sanction imposed in this decision, after seven days' notice in writing, summarily will be suspended or expelled from membership for non-payment. Similarly, the registration of any person associated with a member who fails to pay any fine, costs, or other monetary sanction, after seven days' notice in writing, summarily will be revoked for non-payment.