

This Order has been published by the NASDR Office of Hearing Officers and should be cited as OHO Order 00-15 (C0100003).

**NASD REGULATION, INC.
OFFICE OF HEARING OFFICERS**

DEPARTMENT OF ENFORCEMENT,	:	
	:	
Complainant,	:	Disciplinary Proceeding
	:	No. C01000003
v.	:	
	:	Hearing Officer - EBC
	:	
Respondents.	:	

**ORDER DENYING RESPONDENTS' MOTION SEEKING
LEAVE TO INTRODUCE EXPERT WITNESS TESTIMONY**

Respondents, through their counsel, filed a motion seeking leave to introduce expert witness testimony at the hearing in this proceeding. The Department of Enforcement (Enforcement) filed papers in opposition to the motion. For the reasons set forth below, Respondents' motion is denied.

**I. Factual Background and the
Proposed Expert Witness Testimony**

The Department of Enforcement's Complaint alleges that _____, an NASD member firm, and _____, the Firm's chief executive officer and sole general securities principal, falsely represented, on the Firm's web site and on trade confirmations, the commissions their customers would be charged for trades. According to the Complaint, the Respondents represented that customers would be charged a specific commission rate or that trades would be effected for free when, in fact, they were effecting customer trades on a riskless principal basis through the Firm's proprietary account and charged their customers mark-ups and mark-downs – which were undisclosed – as well as commissions on the trades. More specifically, the First, Fourth, and Seventh Causes allege that, during the period from December 29, 1998 through January 21, 1999, and on February 17 and December 22,

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1999, the Respondents falsely advertised on the World Wide Web the compensation they would receive on customer securities transactions. The Second, Fifth, Eighth, and Tenth Causes allege that, during these periods and on January 5, 2000, the Respondents charged undisclosed mark-ups and mark-downs and made “secret profits” on 316 specific customer trades, and the Third, Sixth, Ninth, and Eleventh Causes allege that, with respect to these trades, Respondents falsely confirmed that the Firm was acting as an agent and charging commissions in accordance with its published commission schedule. Based on the foregoing, Respondents are charged with violating Section 10(b) of the Securities Exchange Act of 1934 (the “Exchange Act”), SEC Rules 10b-5 and 10b-10(a)(ii)(A), and NASD Conduct Rules 2110, 2120, 2210(d)(1)(A) and (B), and 2230. Finally, the Twelfth Cause alleges that the Respondents failed to make appropriate memoranda of brokerage orders in violation of Section 17(a) of the Exchange Act, SEC Rule 17(a)(3), and NASD Conduct Rules 3110 and 2110.

There is no dispute that Respondents committed the violations alleged in the Complaint. In response to Enforcement’s motion for summary disposition, Respondents, through their counsel, admitted the factual allegations against them and that they engaged in conduct that violated NASD and SEC Rules. Further, at a Pre-Hearing Conference on June 8, 2000, counsel clarified that Respondents admit that they violated the specific SEC and NASD provisions set forth in the Complaint, and that the hearing in this matter will be limited to the issue of sanctions.¹

Although Respondents have conceded liability, they seek leave to introduce an expert witness to testify about “certain aspects of the trading practices” they used in order to “show that, despite the violations, the clients of Respondents suffered no financial loss and the Respondents’ undisclosed profits

¹ See Transcript of June 8, 2000 Pre-Hearing Conference.

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did not come at the expense of Respondents' clients." Respondents assert that expert testimony regarding their trading practices is appropriate because it is "unlikely that each of the arbitrators will be an expert in trading matters."

II. Discussion

In NASD disciplinary proceedings, because two of the three Hearing Panelists will have considerable expertise about the securities industry and industry practice, the use of expert witness testimony is far less necessary or routine than it may be in federal court proceedings. Typically, expert witness testimony is not offered in NASD disciplinary matters, unless novel issues or new, complex, or unusual securities products are involved. The fundamental question is whether the proposed testimony would assist the Hearing Panel in understanding the evidence or a fact at issue in the proceeding.

As a threshold matter, the Hearing Officer notes that it is difficult to discern from Respondents' cursory description the substance of the expert testimony they seek to offer. However, it appears Respondents seek to elicit expert testimony to support their affirmative defense "that each of the customers of _____ always received the best Nasdaq bid or offer available at the time of each transaction [and that none of the Firm's customers] paid more for a security purchased from or through _____ than was fair and current or received less for a security sold to or through [the Firm] than was fair and current."²

Putting aside questions of relevance – which the Hearing Officer declines to address at this time – expert testimony is not required to establish that the Respondents charged their customers prices that were favorable in comparison to the prices quoted on Nasdaq at the time of the subject transactions. Respondents easily can prove through documentary evidence the prices at which the subject

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transactions were effected and likewise can establish the then current inside quotations for each of the securities involved. Further, contrary to Respondents' assertion, expertise on trading matters is not required to determine whether the prices they charged were the same as the inside bid or offer quoted on Nasdaq; this would require no more than a simple comparison, which the members of the Hearing Panel clearly would be able to understand without the assistance of expert testimony.

Based on the foregoing, Respondents' motion for leave to introduce expert testimony is denied.

SO ORDERED.

Ellen B. Cohn
Hearing Officer

Dated: New York, New York
July 5, 2000

² Amended Answer, p. 4