BEFORE THE NATIONAL ADJUDICATORY COUNCIL

NASD REGULATION, INC.

In the Matter of District Business Conduct Committee For District No. 8, Complainant, vs. Respondent 1 Respondent.	DECISION Complaint No. C8B960042 District No. 8 Dated: July 22, 1998

Respondent 1 has appealed the September 26, 1997 decision of the District Business Conduct Committee for District No. 8 ("DBCC") pursuant to Procedural Rule 9310. After a review of the entire record in this matter, we find that: from December 14, 1990 to April 30, 1991 (the "Review Period"), Respondent 1, while acting as the Chief Compliance Officer of Firm A was responsible for the overall supervision of Firm A trading activities and that he failed to establish, implement, and enforce supervisory procedures reasonably designed to prevent the customers of Firm A from being charged $419,490 in unfair and fraudulently excessive mark-ups and mark-downs, and unfair and excessive gross commissions, in Company 1 common stock and warrants. We find that Respondent 1 conduct violated Conduct Rules 2110 and 3010.

We order that Respondent 1 be censured, fined $5,000, and required to requalify by examination within 90 days of the date of this decision in all capacities in which he seeks to continue participating in the securities industry. We affirm the assessment of $1,485.75 in DBCC hearing costs and impose $750 in appellate hearing costs.

Background. Respondent 1 entered the securities industry in 1984 as a registered representative. He became a general securities principal in 1987. From July 24, 1990 until early 1992, Respondent 1 was registered with Firm A as a general securities representative, general securities principal, government securities representative, and government securities principal. During this time, Respondent 1 was a Vice-President of the Firm and the Firm's Director of Compliance (also referred to as the Firm's Chief Compliance Officer). Respondent 1 is not presently associated with a member firm.

Facts

During Respondent 1 tenure as Firm A's compliance officer, Firm A public customers were overcharged $419,490 during approximately four months of aftermarket trading in Company 1 securities. The complaint alleged that Respondent 1, who participated in the preparation of Firm A supervisory procedures and also had line supervisory responsibilities, failed reasonably to carry out those responsibilities.

The SEC Complaint. By way of background, on March 29, 1990, before Respondent 1 joined Firm A, the Securities and Exchange Commission ("SEC") filed a Verified Complaint For Injunctive and Other Relief ("the SEC Complaint") against Firm A, two of its principals, its head trader, and its director of sales (the "Defendants") in the United States District Court for the Western District of New York. The SEC Complaint alleged that the Defendants had manipulated the market in 16 offerings underwritten by Firm A by dominating and controlling the markets for these stocks through the use of fraudulent and high-pressure sales techniques to create an artificially large demand for these stocks. The SEC Complaint also alleged that Firm A had generated large profits by purchasing stocks from its customers at low prices and reselling the securities to its customers prior to the completion of the distribution at prices arbitrarily determined by Firm A.

The Court Appointment Consultant 1 and Retention Consultant 2 as Consultants. On April 4, 1990, the Court appointed Consultant 1 as independent counsel to act as a special agent of the Court. Consultant 1 was given the authority to review and report on Firm A policies, procedures, and practices and to make recommendations to improve these policies, procedures, and practices. Specifically, Consultant 1 was given "all powers" necessary and appropriate to: (1) prevent and detect violations of the federal securities laws and the rules and regulations of the appropriate self-regulatory organizations by Firm A and its employees; (2) ensure the maintenance of accurate and adequate books and records; and (3) ensure that Firm A system of internal controls was sufficient to provide reasonable assurances that transactions were executed in accordance with applicable securities laws and regulations. After having determined that he needed the technical expertise of someone familiar with securities markets and broker/dealer regulation, Consultant 1 retained Consultant 2 as his "oversight consultant."

Respondent 1 Association With Firm A. Also in April 1990, Firm A hired Respondent 1 as a consultant to help establish supervisory procedures to be implemented and enforced by Firm A Compliance Department. Respondent 1 testified that his attorney, Attorney 1, (the attorney whose firm represented Respondent 1 in this matter) recruited him initially to act as a consultant for Firm A.[1] In

[1] Respondent 1 sought to have Attorney 1 testify at the DBCC hearing as a fact witness regarding the hiring of Respondent 1 and the details of Respondent 1's employment at Firm A and as a character witness. District staff filed a motion to disqualify Attorney 1’s firm from representing Respondent 1 if Attorney 1 testified. The DBCC hearing panel denied District staff's motion and ruled that Attorney 1 would not be permitted to testify. The hearing panel noted that Respondent 1's attorney

June 1990, Firm A hired Respondent 1 as the Firm's Director of Compliance. During the Review Period, Respondent 1 was the only registered principal in the Compliance Department.[2]

Consultant 1 Submission of New Underwriting Procedures to the Court. On July 3, 1990, Consultant 1 submitted Firm A new underwriting procedures to the Court together with a proposed Order that would allow Firm A to participate in initial and secondary public offerings of Nasdaq-listed companies. Consultant 1 represented that the Firm was very anxious to underwrite the initial public offering ("IPO") of Company A as soon as possible. Consultant 1 stated his belief that Firm A compliance procedures were "sufficient" to underwrite the anticipated IPO of a Nasdaq-listed company. Consultant 1 represented that Consultant 2 would be "intimately involved in any public offering of securities and, among other things, [would] specifically review trading records, Red Herrings, scripts (if used), and [would] spot-check compliance with these procedures by interviewing customers and reviewing whatever records he believes are appropriate."

Pursuant to the underwriting procedures, Consultant 1 was to review Firm A IOI (indications of interest) blotters during the time that IOIs were being solicited, and a "representative of the Compliance Department" was to oversee sales practices in branch offices and provide Consultant 1 with periodic reports. As the effective date of the offering approached, Firm A was to meet with Consultant 1 to discuss the status of the offering and the propriety of further discussions with the issuer in light of all relevant circumstances. Prior to the confirmation date, Consultant 1 was also to review syndicate allocations and copies of "all sold" wires received. A representative of the Compliance Department would be required to monitor and review each of the first three days' trading blotters in all public offerings "to assure compliance with applicable mark-up policies, paying particular attention to interdealer activity and in-house related activity." Consultant 1 was also to review these blotters. Respondent 1 was named in this document as the "Compliance Officer."

-- who was employed by Attorney 1's firm -- had represented that she would be unable to respond to the motion until two days before the hearing. The hearing panel stated that it was unwilling to allow the situation to be unresolved until that time. The panel found that Attorney 1's testimony would be cumulative at best regarding the circumstances of Respondent 1's employment. The panel also decided not to allow Attorney 1 (or anyone else) to act as a character witness. Respondent 1's counsel did not protest these rulings. We agree that it would have been inappropriate to allow Attorney 1 to testify while his firm was acting as Respondent 1's counsel.

[2] On October 2, 1991, after the Review Period, Consultant 1 replaced Consultant 2 with another compliance consultant in response to an expression of SEC concern about Consultant 2's independence and neutrality. Early in 1992, Firm A hired Consultant 2 to act as Compliance Director and reassigned Respondent 1 to Firm A's Research Department.

Respondent 1's Participation in the Preparation of Firm A New Supervisory Procedures Manual. In September 1990, Firm A completed its revised "Home Office Supervisory Procedures Manual." These new procedures were finalized in a document entitled "[Firm A] Home Office Supervisory Procedures Manual" dated September 1990 (the "Manual"). Respondent 1 was identified in the Manual as "Vice President, Director of Compliance, General Securities Principal."

The "Introduction" section of the Manual described the functions of the Firm's Compliance Department. The principal function of the Compliance Department was to supervise the books and record-keeping functions and to supervise all sales, trading and investment banking activities Respondent 1, or a principal designated by him, was responsible for: all supervision in the Firm; reviewing the firm's business mix; determining that all supervisory personnel were properly qualified; and taking and recommending appropriate action in regard to the Firm's supervisory procedures.

The Manual contained a separate section titled "Underwriting Procedures." Particular responsibilities were assigned to specific individuals. For example, the Compliance Officer was to oversee the first due diligence meeting in every offering and spot-check future meetings. Firm A was to maintain a daily blotter of all IOIs, and the Compliance Officer was to review the blotter daily. Each day, Consultant 1 was to be given copies of daily IOI blotters and a summary blotter after IOIs ceased. The Manual provided that:

> A representative of the Compliance Department will be positioned among the branches of the firm overseeing sales practices during this period. Periodic reports of the monitoring process will be generated by the Compliance Department and provided to the special counsel.

The Compliance Department was also specifically responsible for reviewing the syndicate IOI blotter on a daily basis and reviewing and approving all tombstone advertisements. Consultant 1 was designated to receive and review copies of the final underwriting summary blotter prior to the confirmation date, including syndicate allocations and copies of "all sold" wires and copies of the first three days' trading blotters. The Manual designated "areas of special counsel review" as: Red Herring; indications of interest; syndication; final allocation; billing; and beginning of trading.[3]

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[3] Following submission of the new Underwriting Procedures, Consultant 1 received the Court's approval for Firm A to go forward with the Company A offering, which went effective in August 1990. Consultant 1 reported to the Court in September 1990, that Consultant 2 had been present on Firm A's premises two to three days before the effective date and throughout the first two days of aftermarket trading and that no violative conduct had occurred in connection with the offering. Consultant 1 also reported that Firm A had expanded its Compliance Department from two to five individuals to assist Respondent 1. With the Court's permission, Firm A engaged in a secondary distribution of shares in November 1990.

The Company 1 Offering. In November of 1990, Consultant 1 asked the Court to allow Firm A to underwrite the Company 1 IPO. He represented that the offering would be controlled by the Underwriting Procedures that the Court had approved in July. The Court signed an Order giving Firm A permission to underwrite the Company 1 IPO. The Court issued an Order that stated that Firm A could underwrite Company 1 so long as the IPO was in strict compliance with Consultant 1's report and the Underwriting Procedures attached to it. In December, Company 1 completed an IPO of 500,000 units at $6 per unit, with Firm A acting as managing underwriter. Each unit consisted of two shares of common stock and one redeemable common stock purchase warrant. Firm A allocated 24 percent of the offering to an underwriting syndicate and sold the remaining 76 percent to its own customers. Both stock and warrants were traded on The Nasdaq SmallCap Market commencing on December 14, 1990. Firm A made a market in the stock and warrants.

It is undisputed that Firm A dominated and controlled the aftermarket trading in Company 1 stock and warrants during the Review Period. From December 14, 1990 through January 4, 1991, Firm A purchased wholesale 173,300 shares of common stock and 73,200 warrants. By December 28, through inventory and retail accounts, Firm A controlled 90 percent of the public float in Company 1 stock and warrants. From December 18 until April 30, 1991, the end of the Review Period, Firm A controlled at least 87 percent of the float in each instrument. Throughout the Review Period, Firm A accounted for at least 80 percent of the purchase volume and number of transactions, and between 69 percent and 82 percent of the sale volume and number of transactions.

It is also undisputed that, during the Review Period, Firm A executed 1,601 retail trades at unfair prices, with mark-ups and mark-downs ranging from in excess of 5 percent to 28 percent, resulting in excess mark-ups and mark-downs of $419,490. Only 28 of these trades occurred in December 1990; the remaining 1,573 transactions occurred between January 1 and April 30, 1991. Between January and April, the Firm executed 705 unfair mark-ups of common stock and warrants and 868 unfair mark-downs of common stock and warrants.[4] These transactions were executed in violation of the NASD's Mark-Up Policy, Conduct Rule IM-2440.

Discussion

The parties have stipulated to the accuracy of the staff's representation of Firm A aftermarket trading in Company 1. We find, as did the DBCC, that Firm A dominated and controlled the market in Company 1 common stocks and warrants during the Review Period and charged public customers $419,490 in excess mark-ups and mark-downs. The two issues before us are: (1) whether Respondent 1 failed to establish written procedures reasonably designed to prevent Firm A retail customers from being overcharged approximately $400,000 for Company 1 common stock and warrants during the

[4] The next Court-approved offering went effective on April 10, 1991. It was between December 14, 1990 and April 30, 1991, that Firm A controlled and dominated the market in Company 1 common stock and warrants.

Review Period; and (2) whether Respondent 1 failed to carry out his supervisory responsibilities as described in Firm A Manual.

Written Supervisory Procedures. We find that Respondent 1 failed to establish supervisory procedures reasonably designed to ensure that Firm A did not dominate and control the market for Company 1 securities during the Review Period. We find that the Manual did not adequately address the issue of fair pricing in secondary trading. It is evident from our review of the Manual that the supervisory procedures developed by Consultant 1 and Respondent 1 focused on the immediate aftermarket and did not even address the issue of domination and control of aftermarket trading after the first three days.

The Manual contains two sections pertaining to the pricing of securities. The first is entitled "Market Making/Trading." This section pertains to the establishment of quotes by Firm A as a market maker. This section states that a market maker must enter and maintain quotations that are reasonably related to the prevailing market, and it includes a chart of "maximum allowable spreads," but this section does not discuss the pricing of securities to retail customers.

The second section is entitled "Underwriting," and it pertains to the period immediately before, during, and after a public offering. This section requires the Firm's Compliance Offer to monitor and review each of the first three days' trading blotters in all public offerings to assure compliance with applicable mark-up policies, paying particular attention to inter-dealer activity and in-house related activity. The only reference to pricing securities to retail customers states: "All prices to customers shall be fair and reasonable given the circumstances of the trade and at all times relating to the prevailing market prices." We find that this reference is insufficient to meet the requirements of Conduct Rule 3010.

There is no section in the Manual that specifically addresses the fair pricing of securities in the secondary market or the issue of pricing in a dominated and controlled market. We find that this deficiency in the Manual constitutes a violation of Conduct Rules 2110 and 3010. A firm that conducts a retail business must establish procedures that provide guidelines for the fair pricing of securities. Such procedures appear to be contemplated in the "Introduction" section of the Manual, which lists among the principal functions of the Compliance Department the supervision of all sales activities, but the procedures are not discussed in the Manual.

We also find that Respondent 1 bears responsibility for the omissions in the Manual. Respondent 1 was retained as Firm A Director of Compliance in July 1990. Although he did not have sole responsibility for writing the Manual, it is undisputed that he participated in its development and was responsible for reviewing and revising it to make sure that the supervisory procedures were modified in accordance with the changes in the Firm's business mix. The Manual did not contain procedures regarding retail pricing during the Review Period, when the Firm was engaging in such business.

Therefore, we find that Respondent 1, as a Vice-President and principal of the Firm and its Compliance Officer, violated Conduct Rules 2110 and 3010 as alleged.

Supervision of Trading in Company 1 Securities. We also find that Respondent 1 failed to implement and enforce procedures reasonably designed to prevent the Firm's retail customers from being charged unfair and fraudulently excessive mark-ups and mark-downs and unfair and excessive gross commissions in Company 1 common stock and warrants, as alleged in the complaint.

Conduct Rule 3010(2) requires the designation of "appropriately registered principal(s) with authority to carry out the supervisory responsibilities of the member for each type of business in which it engages for which registration as a broker/dealer is required." The Manual, which governed all of Firm A supervisory procedures during the Review Period, assigned this function to the Compliance Department, of which Respondent 1 was the Director. The Manual stated: "The principal function of the Compliance Department is to supervise . . . all sales, trading and investment banking activities." As Director of Compliance, Respondent 1 had this responsibility.[5] The Manual gave Respondent 1 the additional responsibility of "determining that all supervisory personnel are properly qualified."

Notwithstanding that the Manual specifically required the Compliance Department to supervise all sales, trading, and investment banking activities, Respondent 1 purposefully withdrew from any involvement in the supervision of Firm A traders. Respondent 1 contends that Consultant 2 had instructed him "You concentrate on the sales practice, I'll take care of trading," and that if Respondent 1 failed to accede to this instruction, he would have been acting in contempt of court. We find that Respondent 1 contention is not substantiated by the language of the Order itself.

Pursuant to the Order, Consultant 1 was to "have all powers that are necessary and appropriate" to review and report on Firm A policies, procedures, and practices and to make recommendations for improvement thereto. Nowhere does the Court's Order state that Respondent 1 should surrender his supervisory obligations to Consultant 2. Respondent 1 admitted in testimony before the DBCC that during his tenure as Firm A Director of Compliance, his practice was to advise Consultant 2 of any concerns that he had. Thus, we conclude that Respondent 1 failure even to raise these issues with Consultant 2 was unreasonable and that to have raised them would not have been

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[5] We note that the supervisory structures of many firms do not give line supervisory authority to compliance officers. In the instant matter, because the Manual specifically stated that the compliance department was to supervise all sales, trading, and investment banking activities, Respondent 1, as the Director of Compliance, had this supervisory responsibility. By assigning Respondent 1 both supervisory and compliance responsibilities, FAS deprived itself of the benefit of two separate and independent reviews, one by a line supervisor whose function it would have been to carry out the supervisory functions designated in the Firm's procedures manual, and the other by a compliance officer, whose function it would have been to review the Firm's operations through normal surveillance activity.

tantamount to a failure to implement Court-approved recommendations.[6] Respondent 1 would not have violated the Order if he had suggested to Consultant 2, who was not registered with Firm A, that Conduct Rule 3010 and the Firm's supervisory procedures required a registered person to supervise sales and trading activities.

Further, neither the new underwriting procedures nor the supervisory procedures in the Manual contemplated that Consultant 2 would assume total responsibility for monitoring the Firm's activities in the aftermarket beyond the first few days of trading. In fact, Consultant 1 reported to the Court in February 1992 that the underwriting procedures contemplated that " [Consultant 2] would be present in the trading room of Firm A Rochester office, to monitor the trading activity, during the first several days of after-market trading for any IPO underwritten by [Firm A]." Not only was there no indication in the underwriting procedures that Respondent 1 could not also be in the trading room during the immediate aftermarket, the subsequent aftermarket was not even mentioned.[7] We also note that the record does

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[6] We find that cases cited by Respondent 1 do not support his contention that failure to accede to Consultant 2's instructions would have placed him in contempt of court. In SEC v. Data Access Sys., Inc., [1982-1983 Transfer Binder] Fed. Sec.L. Rep. (CCH) & 99,098, at 95,232-233 (D.N.J. 1983), the court held that specific recommendations made by a special agent appointed by the court were not merely advisory guidelines that the respondents could either adopt or spurn. In the instant matter, there was no question regarding the implementation of the Court-approved underwriting procedures. We do not believe that raising the issue of the Firm's obligation to have a registered person supervise trading activities would be comparable to the respondents' refusal in Data Access to acknowledge that the court could order the implementation of the special agent's recommendations.

The court's holding in In re Matter of Credit Suisse First Boston Corp., Exchange Act Rel. No. 39595 (Jan. 29, 1998), likewise does not support Respondent 1's contention that he was powerless to question Consultant 2's instructions. In First Boston, the court permitted the respondent to discuss proposed recommendations with the court-appointed consultant and to propose alternatives, notwithstanding that the firm was required to abide by and adopt the consultant's ultimate recommendations.

[7] In his February 13, 1992 report to the Court, Consultant 1 confirmed that the issue of domination and control following an IPO was beyond his expertise. He advised the Court that he had become aware of issues raised by Firm A's repurchase of securities in the aftermarket as his investigation became "more sophisticated." Consultant 1 noted that although Firm A syndicated in excess of 20 percent of an IPO to a selling group, "in many cases a substantial amount of those securities return to Firm A through its own purchases." Consultant 1 opined that there was nothing inherently wrong with Firm A's purchasing the securities to support the market or to satisfy customer demand, but that if Firm A's registered representatives created the demand, "the question of how they sell the issue may be one that needs to be examined further." Consultant 1 reported:

> The question of whether Firm A improperly dominates and controls the

not contain any evidence of written instructions from Consultant 1 or Consultant 2 that required Respondent 1 to relinquish his supervisory responsibilities to Consultant 2.

The record indicates, in fact, that neither Consultant 2 nor Respondent 1 supervised Firm A traders after the first few days of the Review Period.[8] Consultant 2 refused in testimony before the NASD to take any responsibility for trading or retail sales of Company 1 beyond the immediate aftermarket, and there is no evidence in the record that Respondent 1 even tried to assume supervisory responsibility for that period. When asked whether Firm A had dominated and controlled the market in Company 1 during the Review Period -- December 14, 1990 through April 30, 1991 Consultant 2 stated that he did not think he "would make that representation because I would have to have a basis to make that statement." Consultant 2 also stated that he had never assembled records or made a statistical study of aftermarket trading in Company 1 securities during the remaining days of the Review Period.

In December 1990, Consultant 2 admitted to having difficulty in determining whether the Firm was complying with the NASD's Mark-Up Policy. In a December 18, 1990 memorandum, Consultant 2 asked the President of the Firm, to "[p]lease have the traders indicate somewhere on the trade ticket the inside market, bid and ask, for all Nasdaq transactions done with customers." He stated: "When the markets change, it is almost impossible to determine internally the firm's compliance with the NASD mark up policy." Respondent 1 and Consultant 1 were copied on this memorandum. This indicates to us that Consultant 2 was not, in fact, monitoring Firm A compliance with the NASD Mark-Up Policy after the first few days of the aftermarket. Thus, it appears from the record that no one was monitoring

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> market for certain securities in which it makes a market was an issue in the SEC's underlying complaint. While nothing has come to our attention that would suggest that Firm A is improperly dominating and controlling the market, this is an issue that continues to be of concern to us.

Consultant 1 noted that the issue of domination and control appeared to be "indigenous to the business in general" and "not easily resolved." He stated: "While regulatory agencies may have one interpretation of what constitutes domination and control, a broker/dealer may in good faith have a different interpretation." He noted that Firm A had hired consultants to study the issue, which he described as "beyond our ability to analyze and comment upon." Consultant 1 concluded: "It is more appropriately left to a regulatory agency."

[8] We note that the Complainant sought to establish dates on which Consultant 2 was on Firm A’s premises by means of Consultant 2's reimbursement requests. It was not established, however, that these reimbursement requests were for each date on which Consultant 2 was on Firm A's premises. We not find these reimbursement requests to be probative of Consultant 2's lack of involvement in monitoring secondary trading in Company 1 securities beyond the first three days of the Review Period.

whether Firm A was dominating and controlling the market in Company 1 securities, and no one was examining the fairness of mark-ups in Company 1 common stock and warrants beyond the first few days of the Review Period.

Further, Respondent 1 contention that he had no choice but to follow Consultant 2 instructions to "concentrate on sales practices" is irrelevant to whether his other supervisory responsibilities should have led him to discover that Firm A was dominating and controlling the market in Company 1 securities during the Review Period. Respondent 1 seems not to understand that the key to determining whether a firm is dominating and controlling a market is identification of the source of stock being sold to retail customers. Had Respondent 1 actually supervised the sales practices of Firm A salespersons during the Review Period as he contends Consultant 2 instructed him to do, he would have seen that the order flow in Company 1 securities was coming from the Firm's own customers and not from inter-dealer trades. He would have seen the size of the mark-ups, mark-downs, and commissions. He then could have inquired as to the percentage of the float that was controlled by the Firm.

Respondent 1 should also have been able to ascertain the excessive prices being charged retail customers from his review of documents generated by the Firm in the ordinary course of business. Nowhere in the record does Respondent 1 discuss the results of his review of order tickets, confirmations, account statements, or commission runs. Had Respondent 1 actually reviewed reports that showed gross commission credits to sales representatives, he would have seen that the net percentage of commissions being paid to Firm A salespersons was too high. He then could have ascertained not only that Firm A was dominating the market in Company 1 securities, but also that the prices charged retail customers impermissibly based on quotations that were not substantiated by inter-dealer trades, instead of being based on the Firm's contemporaneous costs.[9]

We find that Respondent 1 would have been acting reasonably as an officer of the Firm and its Director of Compliance to discuss supervision of trading and retail sales with Consultant 2 and Consultant 1, to advise them that the Firm would be in contravention of NASD regulations if he abdicated his supervisory responsibilities to an unregistered person, to insist on carrying out his supervisory obligations, and to petition the Court if they refused. We find that Respondent 1 had an obligation to take these steps.

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[9] It is well established that if a firm's traders are operating in a dominated and controlled market, the firm's retail salespersons are obligated to mark up from the firm's contemporaneous cost. In re Alstead, Dempsey & Co., 47 S.E.C. 1034 (1984) (quotations for obscure securities with limited inter-dealer trading activity may have little value as evidence of the current market and are likely to be subject to negotiation); In re James E. Ryan, 47 S.E.C. 759 (1982), aff'd, 709 F.2d 1518 (9th Cir. 1983) (quotations not a reliable guide to prevailing market price where dealers are consistently able to purchase securities for less).

Respondent 1 knew that he was responsible for compliance in a firm with a significant regulatory history of fraud during the preceding four years -- a firm that could only conduct underwritings under the supervision of a federal court. Respondent 1 testified that he accepted the position as a challenge. A significant part of this challenge was to provide supervision that was reasonably designed to achieve compliance with the NASD's Mark-Up Policy. For the reasons stated above, we find that Respondent 1 failed to do so.

Sanctions

The DBCC imposed a censure, $5,000 fine, and requirement that Respondent 1 requalify by examination in all capacities in which he seeks to participate in the securities industry within 90 days of the date of this decision. We affirm those sanctions.

In determining to affirm the sanctions imposed by the DBCC, we have carefully considered the totality of circumstances under which Respondent 1 operated as Chief Compliance Officer. Although we recognize that Respondent 1 was operating under unusual circumstances, we do not excuse his failure to supervise the Firm's traders and retail salespersons during the Review Period, which permitted Firm A public customers to be overcharged more than $400,000. Consultant 1 intended that Consultant 2 be present in Firm A trading room during the immediate aftermarket of the offerings underwritten by Firm A in the months following the Order. Even if Respondent 1 believed that he should stay out of the trading room during the first few days of aftermarket trading, there is no indication in the record that Consultant 2 continued to observe trading during the remainder of the Review Period. Respondent 1 has no excuse whatsoever for his inaction during that time. Moreover, even if Respondent 1 believed that he should stay out of the trading room, he was not precluded from supervising the Firm's salespersons or reviewing the reports generated by Firm A in a way that was reasonably designed to achieve compliance with applicable securities laws and regulations.

Further, although Respondent 1 was not solely responsible for writing the Firm's Manual, he did participate in its preparation and review, and he was responsible for updating it so that it reflected each of the areas in which Firm A did business. The lack of supervisory procedures regarding secondary trading was a glaring deficiency. It should have been clear to Respondent 1 that Consultant 1 did not have sufficient background to address the issue of mark-ups in a dominated and controlled market, and that Consultant 1 was focusing his attention on Firm A underwriting activities because that was the area in which the misconduct occurred that gave rise to the SEC Complaint and Order. Thus, Respondent 1 was not entitled to rely upon Consultant 1 efforts in this area.

We do not find it mitigating that Respondent 1 was not the only individual responsible for the supervisory failures, or that Respondent 1 appeared to have little influence or authority at the firm. If Respondent 1 believed that he could not properly perform his job under the circumstances, he should have resigned. See, e.g., In re George Lockwood Freeland, 51 S.E.C. 389 (1993) (financial and

operations principal ("FINOP") responsible for performance of his duties as long as he remained firm's FINOP).

The DBCC concluded that Respondent 1 conduct was not egregious, especially compared to that of others at the Firm. We, however, have concluded that Respondent 1 behavior, to the extent that it permitted Firm A salespersons to charge excessive prices for approximately five months, did have serious consequences. On the basis of the facts before us, we find that the sanctions imposed on Respondent 1 by the DBCC are appropriate under the circumstances.

We therefore affirm the censure, $5,000 fine, and requirement to requalify in all capacities in which Respondent 1 seeks to continue participating in the securities industry within 90 days of the date of this decision, or else to cease operating in such capacity until has so requalified. We affirm the assessment of costs of the DBCC proceeding in the amount of $1,485.75, and assess costs of the NAC appeal proceedings in the amount of $750.[10]

On Behalf of the National Adjudicatory Council,

Joan C. Conley, Corporate Secretary

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[10] The recommended sanctions are within those recommended by the NASD Sanction Guideline for supervision.

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, will summarily 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, will summarily be revoked for non-payment.