

NASD OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

ANDREW P. SCHNEIDER
(CRD No. 2907279),

1801 North Flagler Drive
West Palm Beach, FL 33407,

Respondent.

Disciplinary Proceeding
No. C10030088

Hearing Officer—Andrew H. Perkins

HEARING PANEL DECISION

June 29, 2004

Respondent engaged in outside business activity without providing member firm with prompt written notice, in violation of Conduct Rules 3030 and 2110. The Respondent is fined \$5,000 and suspended for 60 days from associating with any member firm in any capacity.

Appearances

Philip Rothman, Regional Counsel, New York, NY (Rory C. Flynn, NASD Chief Litigation Counsel, Washington, DC, Of Counsel) for the Department of Enforcement.

Brian H. Reis, New York, NY, for the Respondent.

DECISION

I. INTRODUCTION

The Department of Enforcement (the “Department”) filed a Complaint on October 23, 2003, against Andrew P. Schneider (“Schneider” or “Respondent”) charging that he engaged in outside business activities without providing his employing NASD member firm with prompt

written notice of his activities, in violation of NASD Conduct Rules 3030 and 2110. Schneider filed an Answer denying the charges and requested a hearing, which was held in New York, NY, on April 15 and 16, 2004, before a Hearing Panel composed of the Hearing Officer, a current member of the District 4 Committee, and a current member of the District 11 Committee.¹

II. FINDINGS OF FACT

A. Background

Schneider began his career in the securities industry in 1997 with Duke & Co., Inc.² Between August 1997 and October 2001, he worked at four other broker-dealers before associating with Millennium Brokerage, L.L.C. (“Millennium” or the “Firm”). Schneider was employed by Millennium from October 26, 2001, until March 21, 2002, during which period he was registered as a General Securities Representative and an Equity Trader.³

According to the Uniform Termination Notice for Securities Industry Registration–Form U-5 that Millennium filed on March 28, 2002,⁴ Millennium discharged Schneider effective March 21, 2002, upon discovering that he had failed to disclose outside business activity and that he had referred customers and business to another broker-dealer. Immediately upon his discharge, Schneider joined Broadband Capital, LLC (“Broadband”).⁵ He was employed by

¹ The hearing transcript for the first hearing day is cited “Tr. I” and for the second hearing day “Tr. II”; the Department’s exhibits are cited as “CX”; and, the Respondent’s exhibits are cited as “R.”

² CX-1, at 2.

³ *Id.* at 3-4.

⁴ CX-2.

⁵ CX-1, at 3.

Broadband from March 21, 2002, until September 11, 2002, where he was registered as a General Securities Representative and an Equity Trader.⁶

Following the disruption caused by the attack on the World Trade Center, Schneider relocated to Florida. In September 2003, he joined STG Secure Trading Group, Inc. where he is currently employed and registered as a General Securities Representative.⁷

NASD commenced the investigation that led to the Complaint in this matter upon receipt of the Form U-5 Millennium filed on Schneider's behalf, which reflected that he had failed to disclose his association with Hedgeco, Inc. ("Hedgeco"),⁸ a new business Schneider incorporated just two days before he joined Millennium.⁹ Schneider was Hedgeco's President.

Schneider formed Hedgeco to organize seminars and operate an educational Internet site for hedge funds in union with Schneider's employing broker-dealer. The purpose of the Internet site and seminars was to forge a relationship with hedge funds and garner their execution business that would be directed to the broker-dealer with which Schneider was associated. Neither Schneider nor Hedgeco would be paid directly for these efforts. Rather, Schneider would earn a commission on the business the hedge funds conducted with his broker-dealer. In other words, Schneider intended Hedgeco to function as a necessary component in a three-part arrangement among Hedgeco, Schneider, and Schneider's broker-dealer.

⁶ *Id.*

⁷ *Id.* at 2. NASD has jurisdiction of this proceeding because the Respondent was registered with NASD at the time of the alleged violation and when the Department filed the Complaint.

⁸ Tr. I, at 286-87; CX-2.

⁹ *See* CX-8, at 4 (Certificate of Incorporation).

Although Schneider formed Hedgeco before he joined Millennium, he failed to disclose that he was Hedgeco's President on the Uniform Application for Securities Industry Registration or Transfer ("Form U-4") he submitted to Millennium.¹⁰ Schneider also did not discuss his plans for Hedgeco with Millennium when he interviewed for his position with the Firm.¹¹ Accordingly, the principals at Millennium were unaware of Hedgeco's existence or Schneider's plans to use Hedgeco as an integral part of his business plan.

B. Schneider's Employment with Millennium

Millennium hired Schneider in October 2001 to help develop its institutional business. Initially, Schneider proposed that he would concentrate his efforts in two areas: trading proprietary accounts and developing institutional business.¹² However, shortly after he joined Millennium, Schneider lost interest in trading and elected to devote all of his time to the development of Millennium's institutional business.¹³

When Schneider joined Millennium, it had a limited number of customers it classified as "institutional." Christopher Horihan ("Horihan"), Millennium's President, testified that the Firm had 10-15 "DVP" accounts that it classified as institutional.¹⁴ The term "DVP," or "delivery versus payment," refers to the securities industry practice, common with institutional accounts, whereby delivery of securities sold is made to the buying customer's bank in exchange for

¹⁰ CX-2, at 5. Form U-4 asks: "Are you currently engaged in any other business either as a proprietor, partner, officer, director, employee, trustee, agent or otherwise?" Schneider answered "No," and he never supplemented his Form U-4 while he was employed by Millennium to disclose that he was the president of Hedgeco. The Department did not charge Schneider with submitting an inaccurate Form U-4.

¹¹ Tr. I, at 36.

¹² *Id.* at 31.

¹³ *Id.* at 35.

¹⁴ *Id.* at 36.

payment, usually in the form of cash.¹⁵ Horihan estimated that a few of Millennium's DVP accounts were small hedge funds and that he considered Schneider's primary responsibility to be the development of additional hedge fund business.¹⁶

Without disclosing Hedgeco's existence, Schneider proposed that he would initiate a seminar program to attract execution business from hedge funds. Under Schneider's plan, Millennium would invite hedge fund managers to present informational seminars to qualified investors. In return, the hedge funds were required to send a certain amount of execution business to Millennium.¹⁷ Schneider's compensation would be based on the amount of execution business he originated.¹⁸ In short, Schneider proposed essentially the same business plan to Millennium as he had developed for Hedgeco.

Horihan testified that he and his partner Steve Fox ("Fox") liked Schneider's plan¹⁹ and that they hired Schneider to implement this strategy.

Schneider started at Millennium on October 26, 2001, whereupon he quickly recruited PP, a Millennium registered representative, to help with the seminar program. Schneider and PP both worked at Millennium's Park Avenue office in New York City. PP, who had approximately four years experience in the securities industry, had been with Millennium for a little more than a

¹⁵ BARRON'S DICTIONARY OF FINANCE AND INVESTMENT TERMS 133 (4th ed. 1995).

¹⁶ Tr. I, at 36.

¹⁷ *Id.* at 35.

¹⁸ Schneider testified that he was to receive everything above two cents per share. (Tr. II, at 14.)

¹⁹ Tr. I, at 33-34.

year when Schneider arrived.²⁰ Also at Millennium's office were one or two traders and an intern.²¹

Between October 2001 and March 2002, Schneider and PP organized and presented six or seven seminars, which Millennium sponsored.²² Horihan was pleased with Schneider's performance and considered the seminar program a success. In his estimation, the seminars generated between \$15,000 and \$25,000 per month in execution business.²³

Schneider, however, was not pleased with Millennium. Horihan and Fox had not settled on the terms of Schneider's employment contract before he started work, and Schneider was not satisfied with his compensation. He complained that Millennium failed to pay him all he was due.²⁴ In addition, he considered Millennium's infrastructure inadequate to support his activities. PP described the problem of poor communication between the New York and New Jersey offices, which Schneider believed hindered his ability to develop business.²⁵ As a result, by as early as January 2002, Schneider began to look for another firm. In connection with the search, CF, then the Vice President of marketing at BC, referred Schneider to Broadband.²⁶

²⁰ CX-3, at 4.

²¹ Tr. I, at 79, 127-28, 241; Tr. II, at 15. Eventually, Schneider also had the intern working on the seminar program. (Tr. II, at 127-28.) Millennium did not have a compliance officer or branch supervisor at this location. (Tr. I, at 206-07; Tr. II, at 14-15.) Schneider and PP's supervisors, Horihan and Fox, the Firm's compliance officer, Donnie Mertz, all were located at Millennium's main office in New Jersey.

²² Tr. I, at 38.

²³ *Id.* at 38-39.

²⁴ Tr. II, at 33-34.

²⁵ Tr. I, at 203; Tr. II, at 34.

²⁶ Tr. II, at 25.

C. Broadband Capital and Schneider's Outside Business Activities

In February 2002, Schneider and PP met with representatives from Broadband. PP testified that the purpose of these meetings was to determine if Broadband was a better fit and whether Broadband would be willing to invest in Hedgeco.²⁷ At the meetings, Schneider told the principals at Broadband about Hedgeco and his plans to develop Hedgeco's Internet site.

By mid-February, Schneider and Broadband began to work together to promote Schneider's business plan, including the use of Hedgeco to organize and sponsor seminars that were designed to generate execution business for Broadband. The Department introduced a number of emails showing that, in February and March 2002, Schneider was referring customers and potential customers to Broadband.²⁸ On February 14, 2002, Schneider wrote to Philip Wagenheim ("Wagenheim"), Broadband's Vice Chairman: "Also I need to start opening accounts very shortly please call me to explain how you want to do this."²⁹ In another dated March 5, 2002, Wagenheim confirmed that he had opened accounts for The Latin Value Fund and ING Barings F/A/O Barbary Coast and that he was working on opening an account called Main Street Fund.³⁰ Schneider directed those funds to Broadband.

Hedgeco and Schneider's involvement with Broadband is evidenced further by an email Schneider sent to Wagenheim dated March 18, 2002, which summarized how one customer "envisions moving ahead with Hedgeco."³¹ The email states that "when [Schneider is] firmly

²⁷ Tr. I, at 180–82. According to PP, Schneider's negotiations with Broadband lasted about one month. (Tr. I, at 179.)

²⁸ See CX–18.

²⁹ *Id.* at 38.

³⁰ *Id.* at 15.

³¹ *Id.* at 7.

established at Broadband Capital [the customer] will open and trade a personal account.” In addition, the email states that the customer will agree to sponsor seminars and will “launch a new fund using her zero coupon bond strategy that will be the fund to be marketed through Hedgeco.”³² This email demonstrates that Schneider was marketing Hedgeco to potential customers while he was registered with Millennium. Moreover, PP testified that Schneider promoted Hedgeco when he met with fund managers. According to PP, Schneider introduced himself as the President and Chief Executive Officer of Hedgeco and told the managers about Hedgeco and how it could help them with their marketing strategy in the future.³³

At the same time as Schneider was working with Broadband, and unbeknownst to Millennium,³⁴ Schneider worked on developing Hedgeco’s Internet site. Schneider commissioned his brother to build the site and recruited PP to help with the design. Although the evidence is ambiguous regarding the progress Schneider made before he left Millennium, the evidence does show that by February the Internet site contained a few pages of material, including a page listing seminars.³⁵ Moreover, despite Schneider’s contention that none of the links on Hedgeco’s Internet site was operational, an email from TW at Beacon Rock Capital dated February 27, 2002, supports a different conclusion. Her request for contact information at Hedgeco reflects that it originated from: “TW <inquiries@hedgeco.net>” and was sent to

³² *Id.* (emphasis added).

³³ Tr. I, at 211.

³⁴ PP testified that Schneider told him not to mention Hedgeco to the principals at Millennium. (Tr. I, at 162–63.)

³⁵ Schneider contended that some of the seminars listed on Hedgeco’s Internet site were “dummies” that he used to demonstrate what the site would look like once it was operational. However, at least one was a real program scheduled for April 3, 2002, at The City Club in San Francisco. (CX–12; CX–13.)

“Andrew Schneider <inquiries@hedgeco.net>.”³⁶ Schneider could not explain how her inquiry could reflect that she sent it from a Hedgeco address unless she had clicked a link on the Hedgeco Internet site. Further, the Hearing Panel notes that TW included her email address at Beacon Rock Capital as “tw@beaconrock.com.”³⁷ Accordingly, the Hearing Panel finds that, by late February 2002, Hedgeco’s Internet site did have the ability to refer inquiries to Schneider.

The Hearing Panel also notes that Schneider conducted much of his business using a Hedgeco email account, aschneider@hedgeco.net, that was set to display Schneider’s status as Hedgeco’s President and Chief Executive Officer.³⁸ Thus, through his email communications, recipients received the impression that he was conducting business on behalf of Hedgeco although Schneider testified that the inclusion of his titles as Hedgeco’s President and Chief Executive Officer on his emails was a mistake.³⁹ Likewise, Schneider testified that anyone who thought they were doing business with Hedgeco was mistaken.⁴⁰ However, Schneider produced no evidence that he took any steps to correct these “errors.” Accordingly, the Hearing Panel rejects Schneider’s explanation and finds that he intentionally used the Hedgeco email account to develop business for himself and Hedgeco.

III. CONCLUSIONS OF LAW

NASD Conduct Rule 3030 prohibits all persons associated with a member firm in any capacity from accepting employment or compensation from any other person because of business

³⁶ CX-18, at 25.

³⁷ *Id.*

³⁸ Schneider also gave PP a Hedgeco email account.

³⁹ Schneider testified that his brother just assumed that he was the President and Chief Executive Officer. (Tr. II, at 72.)

⁴⁰ *See* Tr. II, at 52, 138–39, 142–43.

activity outside the scope of the employment relationship with a member firm unless they provide prompt written notice of the activity to the member firm.

Here, the Respondent first contends that Conduct Rule 3030 does not apply because Hedgeco was nothing more than a “skeleton of a business model” without operations, and Hedgeco did not employ him.⁴¹ In this regard, Schneider emphasized that Hedgeco’s Internet site was under development while he was at Millennium. Second, the Respondent contends that he did not violate NASD Conduct Rule 2110 because any effort he made to facilitate relationships with hedge fund managers was undertaken for Millennium’s benefit.⁴² Schneider argues that he only referred business to Broadband that Millennium could not accommodate.⁴³ Schneider contends that Millennium’s clearing firm would not allow Millennium to undertake certain business such as offshore accounts. In sum, Schneider views his relationship with Broadband as complementing his efforts for Millennium.

The Hearing Panel rejects Schneider’s arguments and finds that for the purposes of Conduct Rule 3030 Schneider was “employed by” Hedgeco, and he therefore was required to notify Millennium of his activities.

In 1988, when the NASD Board of Governors proposed Article III, Section 43 of the NASD Rules of Fair Practice, now Conduct Rule 3030, the Board concluded that “it was appropriate for member firms to receive prompt notification of all outside business activities of their associated persons so that the member’s objections, if any, to such activities could be raised

⁴¹ Respondent’s Pre-Hearing Br. at 2; Tr. II, at 28–29. The Department concedes that it cannot show that Schneider received any direct compensation for his outside business activities.

⁴² Respondent’s Pre-Hearing Br. at 2

⁴³ Tr. II, at 31, 38, 47.

at a meaningful time and so that appropriate supervision could be exercised under applicable law.”⁴⁴ NASD adopted the Rule to prevent harm to the investing public and to limit member firms’ entanglements in legal difficulties that can result from unsupervised outside business activities, which may be unrelated to the securities industry.⁴⁵ In light of these important protective goals, engaging in unreported outside business activities is considered a serious violation.

To realize the important purposes of Conduct Rule 3030, the term “employed by” must be interpreted broadly to refer to the status relationship between an associated person and another.⁴⁶ The scope of Rule 3030 is not limited to the traditional master-servant relationship as understood by common-law agency doctrine. Consequently, Schneider’s status as the President of Hedgeco triggered Conduct Rule 3030’s reporting requirement.

Moreover, Schneider’s involvement with Hedgeco was not static. Schneider was not Hedgeco’s President in name only; he actively pursued Hedgeco’s business objectives. As discussed above, Schneider undertook a variety of business activities for Hedgeco’s benefit. Schneider developed a business plan, commissioned others to develop its Internet site, and promoted Hedgeco to potential customers and business partners. Although neither Hedgeco nor Schneider earned any money from these activities, Schneider nevertheless undertook them for

⁴⁴ *Proposed Rule Change by NASD Relating to Outside Business Activities of Associated Persons*, Exchange Act Release No 26,063, 1988 SEC LEXIS 1841 (Sept. 6, 1988); Notice to Members 88–86, 1988 NASD LEXIS 207 (Nov. 1988).

⁴⁵ See Notice to Members 88–86, 1988 NASD LEXIS 207 (Nov. 1988). See also, e.g., *District Bus. Conduct Comm. v. Micah C. Douglas*, Nos. C06920046 and C06930068, 1995 NASD Discip. LEXIS 217, at *18 (N.A.C. Sept. 19, 1995).

⁴⁶ *Cf.*, NASD Rule 0113 that states: “The Rules shall be interpreted in such manner as will aid in effectuating the purposes and business of the Association, and so as to require that all practices in connection with the investment banking and securities business shall be just, reasonable and not unfairly discriminatory.” The Securities and

his and Hedgeco's mutual benefit. Without question, Schneider formed and promoted Hedgeco with the expectation that he would be compensated from the resulting execution business done by Broadband. The fact that his efforts had not yet yielded a financial return does not exempt his activities from the coverage of Conduct Rule 3030.

Accordingly, considering all of the evidence, the Hearing Panel finds that Schneider's involvement with Hedgeco was an outside business activity about which he failed to provide the requisite notice to Millennium, in violation of NASD Conduct Rules 3030 and 2110, as alleged in the Complaint.

IV. SANCTIONS

For violation of Conduct Rules 2110 and 3030 that do not involve aggravating circumstances, the NASD Sanction Guidelines recommend a fine of \$2,500 to \$50,000 and a suspension of up to 30 business days. When the outside business activities involve aggravating conduct, the Guidelines provide for a longer suspension of up to one year. Finally, in egregious cases, such as those involving a significant injury to customers, the Guidelines provide for a bar.⁴⁷ Citing what it considers aggravating circumstances, the Department seeks a fine of \$10,000 and a six-month suspension. The Department stresses that Schneider was directing business to another broker-dealer, he concealed his outside business activities, and he refused to take responsibility for his actions.

The Hearing Panel begins its analysis with the Principal Considerations listed in the applicable Sanction Guideline. First, the Hearing Panel notes that Schneider's outside activity

Exchange Commission has construed Conduct Rule 3040 similarly. *See, e.g., Charles A. Roth*, 50 S.E.C. 1147, 1150 (1992).

⁴⁷ NASD Notices to Members 03-65, 2003 NASD LEXIS 75, at * 8 (Oct. 28, 2003).

involved some Millennium customers. This is a significant aggravating factor. When NASD recently amended the Sanction Guideline governing violations of Conduct Rule 3030, NASD noted that it did so to stress the importance of determining whether the outside activity involved customers of the respondent's firm and whether the respondent's marketing activities could have created the impression that his firm approved the subject product or service.⁴⁸ Here, Schneider's activity on behalf of Hedgeco paralleled his responsibilities at Millennium. In addition, he used Millennium's office, telephone number, and employees in developing business for Hedgeco and Broadband. These circumstances may well have created the impression that Millennium approved of his activity.

Second, the Hearing Panel notes that Schneider concealed his activity from Millennium, and he instructed PP to keep quiet about Hedgeco. In addition, the Hearing Panel finds that Schneider misrepresented his activities with Broadband in his testimony at the hearing. The evidence shows clearly that once Schneider determined that he was going to leave Millennium, he began to send business and business opportunities to Broadband. Contrary to Schneider's assertions, this activity was not done to benefit Millennium. Indeed, PP indicated that they had reached an agreement to join Broadband before Millennium discharged them. This explains how they were able to begin their employment at Broadband the next day.

Taking these aggravating factors into account, the Hearing Panel concludes that appropriate remedial sanctions are a \$5,000 fine and a 60-day suspension in all capacities.

⁴⁸ *Id.*

V. ORDER

Therefore, having considered all the evidence,⁴⁹ Andrew P. Schneider is fined \$5,000 and suspended for 60 days from associating with any member firm in any capacity.

The foregoing sanctions shall become effective on a date set by the NASD, but not earlier than 30 days after this Decision becomes the final disciplinary action of the NASD; except, if this Decision becomes the final disciplinary action of the NASD, the suspension shall become effective on September 6, 2004, and end at the close of business on November 4, 2004.

In addition, Schneider shall pay costs of \$4,239.36, including an administrative fee of \$750 and hearing transcript costs of \$3,489.36

Andrew H. Perkins
Hearing Officer
For the Hearing Panel

Copies to:

Brian H. Reis, Esq. (*facsimile and first-class mail*)
Philip Rothman, Esq. (*first-class and electronic mail*)
Andrew P. Schneider (*overnight courier and first-class mail*)
Rory C. Flynn, Esq. (*first-class and electronic mail*)

⁴⁹ The Hearing Panel has considered all of the arguments of the Parties. They are rejected or sustained to the extent they are inconsistent or in accord with the views expressed herein.