NASD OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT, Complainant, v. DANA N. FRANKFORT (CRD No. 2243930), Respondent.	Disciplinary Proceeding No. C02040032 **HEARING PANEL DECISION** Hearing Officer - SW Dated: February 1, 2006

Respondent is barred for: (i) omitting material information when soliciting the purchase of securities, in violation of Section 10(b) of the Exchange Act, SEC Rule 10b-5 thereunder, and NASD Conduct Rules 2120 and 2110; (ii) making an unsuitable recommendation, in violation of NASD Conduct Rules 2310 and 2110; and (iii) engaging in private securities transactions, in violation of NASD Conduct Rules 3040 and 2110.

Appearances

Cynthia A. Kittle, Esq., Senior Regional Counsel, Los Angeles, CA, and Roger D. Hogoboom, Esq., Assistant Chief Litigation Counsel, Denver, CO, for the Department of Enforcement.

H. Thomas Fehn, Esq., and Elizabeth Lowery, Esq.,[1] Los Angeles, CA, for Respondent Dana N. Frankfort.

DECISION

I. PROCEDURAL BACKGROUND

On August 16, 2004, the Department of Enforcement ("Enforcement") filed a three-count Complaint against Respondent Dana N. Frankfort ("Respondent"), which was subsequently

[1] Subsequent to the Hearing, Ms. Lowery left the law firm of Fields, Fehn & Sherwin, and was replaced in this proceeding by Gregory J. Sherwin, Esq.

amended on April 18, 2005.[2] The amended three-count Complaint sets forth allegations of misconduct surrounding Respondent's offer and sale of limited partnership interests in a private option fund titled Summit Asset Fund, L.P. ("Summit Fund" or the "Fund").

Count one of the Complaint alleges that Respondent solicited two customers, SW and MHC, through MHC's son DC, to purchase interests in the Fund without disclosing certain material information about Summit Fund, in violation of Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act"), SEC Rule 10b-5 thereunder, and NASD Conduct Rules 2110 and 2120.

Count two of the Complaint alleges that Respondent recommended that SW and MHC purchase the interests in the Fund without having reasonable grounds for believing that the recommendation was suitable for the customers, in violation of NASD Conduct Rules 2110 and 2310.

Count three of the Complaint alleges that Respondent participated in the sale of interests in the Fund to customers SW and MHC, without obtaining the prior approval of his employer, Brookstreet Securities Corp. ("Brookstreet"), in violation of NASD Conduct Rules 2110 and 3040.

Respondent denied that he violated NASD Conduct Rules. Count one of the Complaint specifically alleges that, when soliciting SW and MHC to purchase the Fund, Respondent intentionally or recklessly failed to disclose material information that: (i) the Fund had

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[2] On April 13, 2005, the Hearing Officer granted Enforcement's April 12, 2005 request for leave to amend its Complaint. The Complaint was amended to correct a typographical error in paragraph 6 of the Complaint by deleting the words "equity index," from the sentence "On or about March 3, 2000, Fund commenced trading equity index options for the benefit of its limited partners."

experienced significant operating losses; and (ii) the Fund intended to re-purchase the $450,000 limited partnership interest of RS, the trustee of customer CE's trust, in contravention of the Fund's terms of withdrawal. Respondent denied that he intentionally withheld material information, arguing that he did not know that: (i) Summit Fund had experienced significant financial losses; or (ii) RS's $450,000 would be treated as a limited partnership investment, included in the Fund's trading account, or would be withdrawn.

With respect to count two of the Complaint, Respondent argued that, based on SW's and MHC's financial condition, he had reason to believe that the investment was suitable for them.

With respect to count three of the Complaint, Respondent stated that: (i) when he solicited MHC's investment in the Fund, he did not realize that his association with Brookstreet was effective; (ii) when he initially solicited SW's investment in the Fund, Respondent was not associated with Brookstreet; and (iii) when SW's funds were transferred to the Fund, Brookstreet approved the transaction.

On May 24-27, 2005, the Extended Hearing Panel, composed of an NASD Hearing Officer and two former members of the District 3 Committee, held a Hearing on the allegations of the Complaint in Los Angeles, California.[3] On July 29, 2005, Enforcement filed a post-hearing brief. On September 9, 2005, after requesting and receiving two extensions, Respondent filed his post-hearing brief, in conjunction with a separate motion to dismiss.[4]

Herein below, the Hearing Panel sets forth its findings that Respondent: (i) committed fraud; (ii) made an unsuitable recommendation; and (iii) participated in private securities

[3] Hereinafter, "Tr." refers to the transcript of the Hearing held on May 24-27, 2005; "JX" refers to the Parties' joint exhibits; "CX" refers to Complainant's exhibits; "RX" refers to Respondent's exhibits; and "Stip." refers to the amended Stipulations filed by the Parties on May 27, 2005.

transactions while associated with Brookstreet. The Hearing Panel also denied Respondent's motion to dismiss in a separate order issued simultaneously with this Decision.

II. FINDINGS OF FACTS AND CONCLUSIONS OF LAW

A. Jurisdiction

Respondent entered the securities industry in April 1992 when he became employed by Dean Witter Reynolds, Inc. (CX-1, p. 9; Tr. pp. 649-650). On April 13, 2000, Respondent became registered with NASD member Brookstreet as a general securities representative, which registration remains currently in effect. (CX-1, p. 4; Stip. at ¶ 1). Accordingly, NASD has jurisdiction over Respondent.

B. Background

The Hearing Panel found that Respondent (i) withheld material information from MHC and SW, (ii) recommended the Fund to MHC, via her son, although the Fund was not consistent with MHC's investment objectives, and (iii) solicited or facilitated the investment of MHC and SW in the Fund while associated with Brookstreet without providing prior written notice of his activities to Brookstreet.

1. <u>Strategy of the Fund</u>

In 1997, Respondent was a registered securities representative working with another registered representative, JS, at FSC Securities Corporation,[5] when Respondent met an individual

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[4] Enforcement filed an objection to the motion to dismiss on September 30, 2005.

[5] At FSC Securities Corporation, Respondent and registered representative JS shared a joint representative number. (Tr. p. 795).

named Mr. Derakshani. (CX-1, p. 5; CX-54, p. 1; CX-72, p. 1; Tr. p. 439). Mr. Derakshani was a non-registered insurance broker whose office was in the same building as Respondent's office.[6] (Tr. pp. 437, 658).

Subsequently, Respondent became registered as a general securities representative with National Planning Corporation ("National Planning") on November 23, 1998. (CX-1, p. 4). Nonetheless, Respondent maintained a relationship with JS and maintained an office in the same building with Mr. Derakshani.[7] (Tr. pp. 654-655).

Mr. Derakshani and Respondent routinely discussed their similar investment strategy regarding writing put options. (Tr. pp. 443, 658). A put option gives the holder of the option the right to sell a specific quantity, usually 100 shares per option contract, of a stock (the "underlying security") at a specific price (the "strike price") at any time prior to a specified expiration date. (RX-2, p. 61). By contrast, the seller or writer of the put option is obligated to purchase the underlying security at the strike price if the option is exercised before its expiration. (Id.). Because the writer of the put option may incur very substantial losses in the event of a sharp decline in the price of the underlying stock, which may exceed the principal amount of the writer's investment, writing put options is a highly risky investment strategy.[8]

Having been relatively successful implementing their put writing strategy in their personal accounts and for the accounts of certain other investors, Mr. Derakshani and

[6] Mr. Derakshani was an insurance agent who focused on health, life and annuity products. (Tr. p. 436).

[7] National Planning recruited Respondent and JS, and JS became Respondent's branch manager at National Planning. (Tr. pp. 654-655).

[8] The put option writer generally will profit from (i) the premium received upon selling the option if the underlying stock either appreciates or remains close to the same price, and (ii) interest earned on premium while the option position is held. In the event of a drop in the market price of the underlying stock, the writer of the option would suffer losses by being required to purchase the underlying stock at a price above the market price.

Respondent discussed forming a hedge fund to leverage their investment strategy. (Tr. pp. 443, 659).

a. Summit Fund

In 1999, Mr. Derakshani and Respondent reached an understanding that Mr. Derakshani would form a hedge fund. (CX-72, p. 1; Tr. pp. 658-660). With the understanding that Respondent would join the Fund at some point in the future, Respondent initially delayed taking a specific role in the Fund because Respondent was registered with National Planning. (CX-71, p. 1; Tr. pp. 453-454, 714).

In March 1999, Mr. Derakshani formed the limited liability company, Trinity Asset Management, LLC, later known as Summit Asset Management, LLC ("Summit Management").[9] (CX-3; Stip. at ¶ 2). Summit Management's sole managing member was Mr. Derakshani. (CX-3, p. 8). In 1999, Mr. Derakshani became registered as an investment advisor. (Tr. p. 529). In June 1999, Summit Management organized Summit Fund as a limited partnership and became the general partner of the limited partnership.[10] (JX-2; Stip. at ¶ 2).

In the October 2, 1999 Private Placement Memorandum ("1999 PPM") for Summit Fund, the Fund represented that Summit Management had the exclusive power and authority over the management of the Fund, and would manage the Fund's securities portfolio on a daily basis.

[9] The certificate of limited liability company for Trinity Asset Management, LLC, was filed with the State of Delaware on March 9, 1999. (CX-3, p. 1). A certificate of amendment was filed, changing the name of Trinity Asset Management, LLC, to Summit Asset Management, LLC, with the State of Delaware on June 24, 1999. (CX-3, pp. 7-8).

[10] A certificate of limited partnership for Summit Investment Partners, L.P., was filed with the State of Delaware on June 24, 1999. (JX-2, p. 1). On August 3, 1999, a certificate of amendment was filed changing the name of Summit Investment Partners, L.P., to Summit Asset Fund, L.P. (JX-2, p. 5).

(RX-1, p. 4). Mr. Derakshani, as Summit Management's principal executive officer, served as the Fund's portfolio manager on a daily basis. (Id.).

The 1999 PPM stated that the Fund would initially attempt to maximize long-term capital appreciation by trading and investing in "put" options on securities or on various indices. (RX-1, pp. 4, 12). For providing services to the Fund, Summit Management was to receive a fee equal on an annual basis to one percent of the capital account of each limited partner. (RX-1, pp. 5, 14). Summit Management was also to receive 20% of the net profits allocated to each limited partner as an incentive allocation. (RX-1, pp. 5, 14).

The minimum investment for a limited partner in the Fund was $250,000. (RX-1, p. 5). The limited partners were restricted as to when and how much they could withdraw from their investment in the Fund. (RX-1, pp. 6, 23; Tr. p. 502). Specifically, the Summit Fund partnership agreement provided that only limited partners who had been admitted to the partnership for at least one year were permitted to withdraw from the Fund. (RX-1, pp. 6, 23). In addition, a limited partner could withdraw funds only on the last business day of a calendar quarter, only after giving 90 days written notice, and subject to certain dollar limitations, unless the general partner, Summit Management, consented to a deviation from the procedure or limitations. (RX-1, pp. 6, 23, 31).

b. AGL Life Assurance Company

In addition to soliciting individuals to directly invest in the Fund's limited partnership interests via the Fund's PPM, Mr. Derakshani and Respondent established an arrangement whereby an investor could own the Fund through a self-directed, tax deferred annuity provided by AGL Life Assurance Company ("AGL"), a Pennsylvania insurance company. (Tr. pp. 781-782).

Under the AGL policy, an investor would make a minimum $250,000 premium payment to AGL, which would then establish, pursuant to the Pennsylvania Insurance laws, separate accounts for the investor, consisting of a money market account and a managed investment account. (RX-2, p. 1). After payment of the first year $250,000 minimum premium, no additional premiums were required. (RX-2, pp. 1, 9, 15).

AGL drafted a separate PPM dated August 1999 and revised it in February 2000. (RX-2, pp. 1, 34). Just as disclosed in the Fund's 1999 PPM, AGL's PPM disclosed that the managed investment account, managed by Summit Management, would initially attempt to achieve its investment objectives by trading and/or investing in put options on securities or on various indices. (RX-2, p. 28). AGL imposed a charge equal to a percentage of the net assets of the variable account to compensate AGL mortality and expense risks in connection with the policy. (RX-2, p. 20).

In a supplement to its PPM dated March 3, 2000, AGL reported that its managed investment account would be invested in the Summit Fund. (RX-3, p. 1). AGL's PPM had information regarding the Summit Fund, similar to the Fund's 1999 PPM; however, AGL's policy also provided that a limited partner could withdraw from the Fund upon death and during a specific "Free Look" period, generally 10 days after the annuity was established. (RX-2, p. 43). In addition, AGL could terminate Summit Management's agreement to manage the managed investment account without penalty. (RX-2, pp. 46, 77).

2. Respondent's Participation in the Summit Fund

Although Respondent was not listed in any of the 1999 formation documents, Mr. Derakshani and Respondent acted as equal partners in Summit Management, which controlled Summit Fund. (Tr. p. 501). Respondent provided advice and participated in decisions regarding the structure and organization of Summit Fund, including meeting with the attorneys who prepared the Fund's offering documents, meeting with brokers to establish an account to hold the Fund's cash and securities, and interviewing other third parties who would provide services to the Fund. (Tr. pp. 450-452, 484-485). Respondent paid half of the formation expenses for Summit Fund. (Tr. pp. 629, 661; CX-73, p. 153).

In January 2000, Respondent and Mr. Derakshani met with a representative from Fidelity Investments Institutional Brokerage Group ("Fidelity") to explore using the Fidelity platform to execute Summit Fund's option transactions. (Tr. pp. 205-206). On February 15, 2000, Mr. Derakshani, on behalf of Summit Fund, opened an account at Fidelity to implement his strategy of writing put options. (JX-6).

On February 23, 2000, Respondent resigned from National Planning to take a more direct role in Summit Fund.[11] (CX-59, p. 2; Tr. pp. 666-667, 712-713). Respondent was to be primarily responsible for soliciting investors for the Fund, and Mr. Derakshani was to be primarily responsible for the Fund's trading decisions. (Tr. p. 209). Respondent stipulated that during the period October 1999 through July 2000, he provided written or oral information regarding the Fund to potential investors, including but not limited to DC, acting on behalf of MHC, and to

[11] Respondent's actions indicated that he was aware of NASD Conduct Rule 3040's restrictions on private securities transactions.

SW. (Stip. at ¶ 4). Ultimately, Respondent solicited and the Fund received monies from ten investors, including MHC and SW, but excluding RS as trustee for CE. (JX-3, p. 6; CX-67, pp. 2-3; Tr. p. 691-692).

In March and April 2000, Respondent held himself out to the public as a managing senior partner of the Summit Fund, as reflected on a business card that he distributed, letters that he signed, and an outside business activity form that he submitted to Brookstreet. (CX-49, p. 2; CX-50, p. 3; Tr. pp. 491, 705-706, 756, 760). Respondent routinely spoke with Mr. Derakshani regarding Summit Fund's trading and was generally aware of how much money was in the Summit Fund account. (Tr. pp. 460-461, 476, 716-717).

Mr. Derakshani received the Fund's Fidelity account statements, and he had access to the statements online. (JX-6, pp. 5-6). Respondent was not an authorized individual on the Fidelity account and did not have access to the account statements on line. (JX-6, p. 7; Tr. pp. 483, 696). Mr. Derakshani did not provide copies of the Fidelity account statements to Respondent.[12] (Tr. pp. 460-461).

However, Mr. Derakshani told Respondent that the Fund was down at the end of March 2000. (Tr. p. 693). During the March 2000 to June 2000 time frame, Respondent admitted that he was generally aware of the Fund's cash position, equity value, and buying power, having discussed the matters with Mr. Derakshani more than once. (Tr. pp. 695, 818-819). Respondent also admitted that on a number of occasions, he traded in options similar to the option trading

[12] Financial statements were not published for the Fund until November 6, 2000, when Mr. Banerjee, the Fund's accountant, prepared a compilation for the period ending June 30, 2000, and, on November 28, 2000, when Mr. Banerjee prepared a compilation for the period ending September 30, 2000. (RX-7; JX-3; JX-4). These statements reflected significant losses. (JX-3; JX-4).

executed by Mr. Derakshani for the Fund. (Tr. p. 780). At the end of March and April 2000, Respondent was losing money in his own parallel option trading. (Tr. p. 788). Therefore, although Respondent claims that he did not know that Summit Fund had experienced significant financial losses, the Hearing Panel finds that Respondent knew or should have known of the Fund's negative financial performance. (Tr. pp. 692-693).

3. Financial Performance of Summit Fund

a. March 2000

Respondent's aunt and uncle were the initial investors in the Fund, investing $173,000 in the Fund on February 29, 2000.[13] (Tr. pp. 691-692; CX-67, p. 2). Respondent's parents were the second investors in the Fund, investing $1,000,000 on March 1, 2000. (CX-67, p. 2). The Summit Fund's first trade settled on March 3, 2000, just before the stock market began to plummet in value at the end of March 2000. (JX-7, p. 6; Tr. pp. 678, 691).

From March 1 to March 31, 2000, an additional $3,007,428 was added to the Fund's trading account. (JX-7, p. 11). Although the Fund had received $3,180,427 by March 31, 2000 from customers, including $450,000 from RS, the Fund's March 31, 2000 Fidelity account statement reported a one-month loss of $1,108,782, and had a net value of $2,071,646. (JX-7, p. 4; CX-79, p. 4).

b. First Quarter: April through June 2000

As of April 30, 2000, just prior to Respondent soliciting MHC's investment, the ending net value of Summit Fund's trading account was $593,273, representing a loss in excess of 82%

[13] Respondent's aunt and uncle deposited additional funds into the Fund on March 27, 2000 and April 13, 2000, totaling $37,000, to meet the $250,000 minimum investment. (CX-13, p. 1).

or $3,346,428 of the funds that Respondent had raised. (JX-7, p. 13; CX-79, p. 4; Stip. at ¶ 8). As of May 31, 2000, the ending net value of Summit Fund's Fidelity account was $382,214.40. (JX-7, p. 23; Stip. at ¶ 13).

For the three-month and six-month periods ending June 30, 2000, the Fund had a net loss of $1.8 million, and for the year to date ending June 30, 2000, the Fund had a net loss of $2.9 million.[14] (JX-3, p. 4). As of June 30, 2000, the ending net value in the Fidelity account was $1,147,391.43, which included MHC's investment of $400,877.55 on June 20, 2000. (JX-7, pp. 32, 37; Stip. at ¶ 19).

c. July 2000

After June 2000, Mr. Derakshani drastically decreased the number of trades and engaged in minimal transactions in the Fund's account. (Tr. pp. 639-640). As of July 30, 2000, despite total inflows from investors of $2.4 million, not including RS's $450,000, the Fund had a net ending value of $714,191.03.[15] (JX-3, p. 6; JX-7, p. 39; Stip. at ¶ 23).

4. Respondent's Association with Brookstreet

Seeing that the Fund was not the financial success that he had anticipated, in April 2000, Respondent took steps to re-enter the securities business. (Tr. pp. 670, 672). Respondent submitted an employment application to Brookstreet and was interviewed by Stanley Brooks, Brookstreet's president. (CX-50, p. 3; Tr. pp. 117, 119-120). During the interview, Mr. Brooks advised Respondent that, if he accepted employment at Brookstreet, he could no longer participate in the Summit Fund under its present arrangements. (Tr. pp. 120-122, 156; Stip.

[14] On June 1, 2000, another customer, SA, withdrew $15,000 of her original $816,428 investment in Summit Fund via AGL. (CX-79, p. 4; Tr. p. 562).

[15] On August 9, 2000, customer SA withdrew $47,814 Summit Fund via AGL. (CX-79, p. 4).

at ¶ 5). Respondent executed a registered representative contract with Brookstreet on March 28, 2000. (JX-10).

On April 10, 2000, Respondent became associated with Brookstreet when he submitted a signed Form U-4 to Brookstreet. (Tr. p. 727).

5. <u>Return of $450,000 in Monies to Trustee RS</u>

On March 19, 2000, customer CE invested $130,000 in the Summit Fund upon the recommendation of Respondent.[16] (CX-13, p. 1). CE was Respondent's client at National Planning. (Tr. pp. 698, 747). In March 2000, Respondent also solicited RS as trustee of CE's trust to invest in the Fund. (Tr. pp. 697, 700). On March 24, 2000, as a result of discussions with Respondent, RS authorized the wire transfer of $450,000 from the CE trust to the Fund's trading account at Fidelity.[17] (CX-42; Tr. p. 487).

The Fund recorded and deposited the $450,000 into the Fund's trading account on March 31, 2000. (JX-7, p. 11; Stip. at ¶ 7). Respondent represented to RS that RS could get the money back at any time.[18] (CX-38). On June 28, 2000, RS wrote Respondent a letter requesting that Respondent confirm that he was holding the monies in Summit Fund and that he had not transferred the monies to AGL. (CX-39).

On July 9, 2000, at RS's request via Respondent, Mr. Derakshani requested and received a written confirmation from the Fund's broker that the Fund had received $450,000 from RS. (CX-40). On July 17, 2000, RS sent Respondent a letter, instructing Respondent to liquidate his

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[16] Customer CE deposited another $100,000 into the Fund on April 17, 2000. (CX-13, p. 1).

[17] On March 24, 2000, Respondent sent RS a subscription agreement and annuity application for the Summit Fund. (CX-37).

[18] In a March 27, 2000 letter, Respondent wrote RS that if he needed to withdraw the monies, he would be able to do so. (CX-38).

position in the Fund and return the entire proceeds to him immediately. (CX-41). On July 19, 2000, Mr. Derakshani instructed Fidelity to issue a check for $450,000 to RS from the Summit Fund account. (JX-8, p. 1). On July 19, 2000, the Fund distributed $450,000 to RS, just after the Fund received SW's $250,000 on July 7, 2000. (CX-9; JX-7, p. 42).

If RS's monies were properly placed in the Fund's trading account as an investment in the Fund, according to the terms of the limited partnership agreement, RS was not entitled to withdraw the $450,000 from the partnership until a year after the deposit, i.e., March 31, 2001. In addition, RS should have been required to give 90 days prior notice rather than two days notice, and he should have received an amount that took into account the financial results of the Fund during the period. None of these conditions was met.

There is a dispute regarding whether RS wanted the $450,000 to be invested in the Fund, or whether he wanted the monies held until he made a final decision. Mr. Derakshani believed the $450,000 was an investment in the Fund, and initially treated it as such. Certain of the documentation provided by Mr. Derakshani at the Hearing supports Mr. Derakshani's belief.[19] However, there is also evidence that Respondent and RS expected the funds to be held in a suspension account pending RS's determination whether to invest in the Fund.[20] (Tr. p. 742; CX-36). Without the testimony of RS and without any testimony verifying the subscription documents provided by Mr. Derakshani,[21] the Hearing Panel finds that Enforcement failed to

[19] At the Hearing, Mr. Derakshani presented an AGL PPM receipt dated March 24, 2000 and an AGL assignment form dated March 24, 2000, both allegedly signed by RS, which documents suggested, but did not establish, that RS intended to make two investments in the Fund, one through AGL. (CX-84; CX-85).

[20] In a February 27, 2003 letter to the NASD staff, RS wrote that he could not say whether or not he signed a subscription agreement with Summit Fund, and he wrote that he was emphatic that he had advised Respondent that RS wanted the monies returned if he decided "not to finish the investment." (CX-36).

[21] Mr. Derakshani testified that he had no specific recollection of when the documents were received, and he did not recognize RS's signature. (Tr. pp. 559, 580).

establish, by a preponderance of the evidence, that RS intended that his $450,000 be treated as an investment in the Fund.

6. SW and MHC's Summit Fund Investments

a. Customer SW

A friend of Respondent recommended to SW that he contact Respondent. (Tr. p. 682). In April 2000, Respondent met SW, a wealthy Los Angeles, CA, real estate executive, who expressed an interest in Respondent's put option strategy. (Tr. pp. 682-685, 687). Respondent testified that when he initially solicited SW's investment in the Fund, SW wanted to utilize the method in his own account before investing the $250,000 minimum in the Fund. (CX-54, p. 2; Tr. p. 685). On April 26, 2000, SW executed new account documents to open an account with Respondent at Brookstreet. (CX-25, p. 3). During May 2000, Respondent executed option transactions in SW's Brookstreet account, similar to the option transactions executed by Mr. Derakshani in Summit Fund's Fidelity account. (CX-29, pp. 1-6; JX-7, pp. 23-31; Tr. p. 780).

On June 29, 2000, SW authorized Respondent to wire transfer $250,000 from his Brookstreet account to Summit Fund. (CX-27). Respondent attempted to arrange the transfer of $250,000 to the Fund without providing prior written notice to Brookstreet. (Tr. pp. 134, 688-689). Another Brookstreet employee brought the proposed wire transfer to the attention of Mr. Brooks. (Tr. p. 130; Stip. at ¶ 18).

Mr. Brooks decided to authorize the transfer as a one-time exception to his conditions of employing Respondent, i.e., that Respondent no longer have any dealings with the Fund. (JX-10; Tr. p. 131). On July 5, 2000, Brookstreet approved SW's transfer of $250,000 from his Brookstreet account to purchase a limited partnership interest in the Fund. (JX-10; Tr. p. 131). On July 7, 2000, Respondent facilitated the transfer of $250,000 from SW's Brookstreet account to the Summit Fund. (CX- 27, pp. 3-4).

Although as of June 30, 2000, the Fund had suffered a loss of $2.9 million, Respondent admitted that he never provided SW with any financial information about the Fund either at the time of the original recommendation or when he facilitated the deposit of the $250,000 in the Fund. (Tr. pp. 706-707).

b. Customer MHC

On April 30, 2000, Respondent traveled with JS from California to Chicago, IL, to attend a fundraiser organized by MHC's family. (Tr. pp. 40, 44). MHC was JS's client. (Tr. p. 677). JS invested MHC's funds primarily in NASDAQ and some blue chip stocks as well as in five or six annuities. (Tr. pp. 39, 41-42). DC, who is MHC's son, had the responsibility of overseeing the portion of MHC's assets that were managed by JS. (Tr. pp. 36-37, 39). MHC is a wealthy author. (Tr. p. 87).

On May 1, 2000, Respondent met DC for breakfast in Chicago, IL, and solicited DC to invest in the Fund. (Tr. pp. 45-46, 677, 762). DC agreed to rollover the proceeds of two annuities that were not doing as well as other annuities owned by MHC. (Tr. p. 786). The entire Fund presentation took approximately 15 minutes. (Tr. p. 116). Respondent proposed the

Summit Fund as an alternative to the two annuities issued by Pacific Life that were held by MHC and were not performing as expected. (Tr. p. 46).

DC agreed to a make an IRS Rule 1035 variable annuity exchange and signed the papers to authorize the liquation of the two variable annuities and the investment of the proceeds in the Fund. (Tr. pp. 50-51, 53). Respondent did not provide MHC with any financial performance information concerning the Fund, nor did he advise MHC that RS had a special arrangement with the Fund. (Tr. pp. 72, 706-707, 762).

DC testified that he was not aware that by investing in Summit Fund he was investing in a different investment strategy, i.e., that the Fund would primarily engage in options trading. (Tr. pp. 48-49, 83-84, 86). DC believed he was moving from one insurance annuity product to another insurance annuity product. (Tr. p. 84). DC testified that he was not aware that the Fund was a startup having been in existence only two months. (Tr. p. 72). DC testified that Respondent stated that he recommended the AGL annuity to DC because it was better managed and had a better track record than the Pacific Life annuities.[22] (Tr. p. 48). In addition, DC testified that he did not complete the forms that indicated that MHC had an aggressive growth investment objective, and that he would not have chosen that investment objective. (Tr. pp. 55-56). DC also testified that there was no discussion of surrender charges for the annuities that were to be rolled over into the Summit Fund. (Tr. pp. 58-59).

Respondent testified that he did tell DC that the Fund would engage primarily in option trading. (Tr. p. 707). The Hearing Panel found DC to be more credible than Respondent based

[22] Respondent acknowledged that he relied on Mr. Derakshani's statements that he was capable of managing the Summit Fund. (Tr. p. 715).

on the demeanor of DC. DC's testimony was straightforward and offered without hesitation, and DC's description of his conversation was consistent with Respondent providing a brief 15-minute presentation about the Fund. In addition, the Hearing Panel noted that MHC and DC had reached a settlement with Respondent regarding the losses, and accordingly, DC had no incentive to lie about what occurred.[23]

Respondent contacted Mr. Derakshani to arrange to provide MHC with the necessary information for the rollover into the AGL annuity. (Tr. p. 680). Respondent never spoke directly with MHC. (Tr. p. 762). To complete the rollover, DC arranged for Pacific Life to send two checks to AGL totaling $399,868.70, which were deposited into MHC's AGL money market account on May 29, 2000. (CX-23, pp. 97-98, 103). On June 20, 2000, MHC's $400,877.55 proceeds of the AGL money market account were deposited into the Summit Fund. (CX-23, p. 103; Stip. at ¶ 15). Respondent did not provide Brookstreet with prior notice of his intent to solicit the MHC investment. (Tr. p. 134).

7. <u>Termination of the Summit Fund</u>

On December 18, 2000, AGL terminated MHC's investment in Summit Fund and requested that the remaining proceeds of the account be wired to AGL. (CX-23, p. 104). On February 16, 2001, Mr. Derakshani directed Fidelity to wire funds to AGL on behalf of MHC. (CX-23, p. 109). Summit Fund wired $40,926.84 of the original $400,877.55 investment to AGL on behalf of MHC. (Stip. at ¶ 24). In an AGL PPM Supplement dated April 26, 2001, AGL advised its customers that Summit Fund had been removed as a potential investment option for the AGL annuity. (CX-23, p. 70).

[23] On August 20, 2003, MHC entered into a settlement agreement with Respondent and Brookstreet. (CX-24).

In August 2001, Fidelity decided to terminate its relationship with Summit Fund. (Tr. pp. 226-227). On August 23, 2001, Mr. Derakshani directed Fidelity to close the Fund's account and distribute the proceeds of the account to the Fund's limited partners. (CX-8). SW received $22,918.99 from his $250,000 investment. (Stip. at ¶ 25). SW reached a settlement agreement with Brookstreet regarding his Brookstreet account and the Summit Fund investment for $325,000. (Tr. p. 151; Stip. at ¶ 36).

Effective August 20, 2003, MHC, Brookstreet and Respondent reached a settlement agreement whereby Brookstreet paid MHC $100,000 and Respondent was to pay MHC $100,000 in monthly payments of $4,166.67.[24] (CX-24).

C. Count One: Respondent's Failure to Disclose the Fund's Financial Performance to SW and MHC Constituted Fraud

Count one of the Complaint alleges that Respondent violated Section 10(b) of the Exchange Act, SEC Rule 10b-5 thereunder, and NASD Rules 2120 and 2110 when he committed fraud by failing to disclose to customers MHC and SW that Summit Fund: (1) had realized significant market losses; and (2) intended to re-purchase the limited partnership interest of RS in contravention of the terms of the PPM.

Section 10(b) of the Exchange Act[25] makes it unlawful "to use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance in contravention" of the SEC rules and regulations.

SEC Rule 10b-5 provides in part that "[i]t shall be unlawful for any person, directly or indirectly, . . . (b) to make any untrue statement of a material fact or to omit to state a material

[24] As of the May 2005 Hearing, Respondent had two remaining monthly payments to complete his settlement obligation to MHC. (Tr. p. 282).

fact necessary in order to make the statement made, in light of the circumstances under which they were made, not misleading."

Conduct Rule 2120, NASD's anti-fraud rule, 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.[26]

In order to find a violation of Section 10(b) of the Exchange Act, SEC Rule 10b-5 thereunder, and Rule 2120, there must be a showing that: (1) misrepresentations and/or omissions were made; (2) the misrepresentations and/or omissions were material; (3) the misrepresentations and/or omissions were made with requisite intent, i.e., scienter;[27] and (4) the misrepresentations and/or omissions were made in connection with the purchase or sale of securities.[28]

A number of the relevant facts are not in dispute. The Fund experienced significant losses from it inception, and Respondent did not disclose the Fund's negative financial performance when he solicited SW and MHC, or when he facilitated the transfer of their funds to the Summit Fund. The issues to be decided are (i) was omission of the Fund's negative financial performance made in connection with the purchase and sale of a security, (ii) was the Fund's negative financial performance material information, and (iii) did Respondent act with scienter when he omitted the negative information.

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[25] 15 U.S.C. §78(j)(b).

[26] Prime Investors, Inc., Exchange Act Release No. 38487, 1997 SEC LEXIS 761, at *24 (Apr. 8, 1997) (making material misstatements of fact in connection with a sale of a security is a violation of Conduct Rule 2120).

[27] See Aaron v. SEC, 446 U.S. 680, 686-87, n. 5 (1980); Ernst v. Hochfelder, 425 U.S. 185, 193 (1976).

[28] For Section 10(b) of the Exchange Act and SEC Rule 10b-5 thereunder, the transactions must also involve interstate commerce or the mails, or a national securities exchange. Respondent used a means and instrumentality

The "in connection with" requirement of Section 10(b) of the Exchange Act has been construed broadly to include any statement that is reasonably calculated to influence the average investor to purchase or sell a security.[29] Limited partnership interests are investment contracts, and thus "securities" within the meaning of Section 3(a)(10) of the Exchange Act.[30] There can be no dispute that Respondent's omissions regarding the disappointing financial performance of Summit Fund would have influenced the average investor's decision to purchase the Fund, and accordingly, Respondent's omission occurred in connection with the purchase or sale of a security.

Liability for an omission arises only if, under the circumstances, failure to disclose a fact is misleading. A duty to disclose occurs when, in light of the statements made and the surrounding circumstances, disclosure of particular facts is necessary to avoid misleading impressions.[31] A registered representative, as a securities professional, has an obligation to disclose known material facts or material facts that were "reasonably ascertainable."[32]

Facts are material if there is a substantial likelihood that a reasonable investor would consider them important in making an investment decision and would view disclosure of them as significantly altering the total mix of information made available.[33] There can no dispute that the information concerning the disappointing financial performance of Summit Fund would have

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of interstate commerce when he facilitated the transactions via telephone and U.S. mail. See SEC v. Hasho, 784 F. Supp. 1059, 1106 (S.D.N.Y. 1992), 1992 U.S. Dist. LEXIS 1322 at **148-149 (S.D.N.Y. Feb. 14, 1992).

[29] Hasho at 1110 ("any statement that is reasonably calculated to influence the average investor satisfies the 'in connection with' requirement of Rule 10b-5").

[30] 15 U.S.C. §78c(a)(1).

[31] Brody v. Transitional Hospitals Corp., 280 F.3d 997, 1006 (9th Cir. 2002).

[32] Hanley v. SEC, 415 F.2d 589, 597 (2nd Cir. 1969).

significantly altered the total mix of information made available to a reasonable investor and was, therefore, a material fact.[34] The material fact of the Fund's dismal financial performance was also "reasonably ascertainable" to Respondent, as Mr. Derakshani's de facto partner.

Respondent had numerous red flags, including his individual trading of options and his discussions with Mr. Derakshani, to alert him that he should obtain specific details about the Fund's performance. Respondent admitted that by the end of March 2000, he knew that the markets were imploding and that the Fund was going down in value. (Tr. p. 719). Accordingly, the Hearing Panel finds that the financial performance of the Fund was material information, which Respondent had access to and which he should have disclosed when he recommended the purchase of the Fund.[35]

Scienter is established by a showing that a respondent acted intentionally or with severe recklessness. Severe recklessness is limited to those highly unreasonable omissions or misrepresentations that involve not merely simple or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and that present a danger of misleading buyers or sellers which is either known to a respondent or is so obvious that a respondent must have been aware of it.[36]

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[33] Basic Inc. v. Levinson, 485 U.S. 224 at 231-232 (1988); TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976).

[34] Even if Respondent had a sincere expectation that the market would rebound, and the Fund's 82% marked-to-market losses would not be realized, Respondent was still obligated to disclose the losses as material information to the investors because it was the investors' decision, rather than Respondent's, to put their faith in the market rebounding.

[35] Richard J. Puccio, Exchange Act Rel. No. 37849 (Oct. 22, 1996) (broker failed to provide any negative information about stocks he recommended, thereby violating the antifraud provisions); V.F. Minton Securities, Inc., 51 S.E.C. 346, 351 (1993), aff'd mem., 18 F.3d 937 (5th Cir. 1994) (a broker's recommendation implies that he has done a reasonable investigation and that his recommendation is based on such investigation).

[36] See Tuchman v. DSC Communications Corp., 14 F.3d 1061, 1067 (5th Cir. 1994), 1994 U.S. App. LEXIS 3326, at *14 (5th Cir. Feb. 24, 1994).

The Hearing Panel finds that Respondent was aware that neither SW nor MHC would have invested in the Fund had Respondent been honest about the then current financial situation of the Fund, and that he intentionally did not advise them of the Fund's financial condition. Accordingly, the Hearing Panel finds that Respondent acted with scienter. Consequently, the Hearing Panel finds that Respondent's conduct constituted fraud in violation of Section 10(b) of the Exchange Act, SEC Rule 10b-5 thereunder, and NASD Conduct Rules 2120 and 2110.

The Hearing Panel does not find that Enforcement proved by a preponderance of the evidence that Respondent knew or should have known that RS would demand repayment of CE trust's $450,000 in July 2000, monies which had not been properly segregated, when Respondent solicited the funds of SW in March 2000 and MHC in May 2000, or when the funds were actually invested (MHC in June 2000 and SW in July 2000).[37] Accordingly, the Hearing Panel does not find that Respondent's failure to advise SW and MHC of the $450,000 repayment constituted fraud.[38]

[37] The 1999 PPM specifically stated that the general partner could consent to deviations from the withdrawal terms of the partnership, and no representations were made concerning the size of the Fund. (Tr. p. 791; RX-1, p. 23).

[38] The Hearing Panel decided that, without the testimony of RS, it would not give undue weight to the documents provided late in the Hearing by Mr. Derakshani that supported his view that RS intended to invest in the Fund. (CX-84; CX-85).

D. Count Two: Fund was an Unsuitable Recommendation for Customer MHC

Count two of the Complaint alleges that Respondent did not have a reasonable basis for believing that the Fund was a suitable investment to either MHC or SW because it had experienced substantial losses, and therefore Respondent violated NASD Conduct Rules 2310 and 2110.

NASD Conduct Rule 2310(a) provides that, in recommending to a customer the purchase of a security, a representative must have "reasonable grounds for believing that the recommendation is suitable for such customer based on the customer's other security holdings and financial situation and needs."[39] "The test for whether [the broker's] recommended investments were suitable is not whether [the customer] acquiesced in them, but whether [the broker's] recommendations . . . were consistent with [the customer's] financial situation and needs."[40] To ensure that the representative can make this determination, Rule 2310(b) requires reasonable efforts to obtain information concerning, among other things, the customer's financial status, tax status, and investment objectives.[41]

Most commonly, the suitability rule is violated by a recommendation that might be suitable for some investors but is unsuitable for a specific investor to whom the recommendation is directed. It is possible, however, that a particular investment – for example, a fraud—would be unsuitable for any investor, regardless of the investor's wealth, willingness to bear risk, age, or other individual characteristics.[42]

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[39] District Bus. Conduct Comm. v. McNabb, No. C01970021, 1999 WL 515761, at *13 (N.A.C. Mar. 31, 1999).

[40] Wendell D. Belden, Exchange Act Rel. No. 47859, 2003 SEC LEXIS 1154 (May 14, 2003).

[41] Hanley at 597 (2d Cir. 1969) (a broker-dealer cannot recommend a security unless there is an adequate and reasonable basis for such recommendation).

[42] F.J. Kaufman, Exchange Act Rel. No. 27535, 1989 SEC LEXIS 2376 (Dec. 13, 1989).

At the Hearing, Enforcement argued that, because of the market's continued downturn, as of May 1, 2000, an investment in Summit Fund fell into this latter category, and was unsuitable for <u>anyone</u>. The Hearing Panel does not find that, as of May 1, 2000, Respondent believed, knew, or should have known that the market would continue its downturn, and that the Fund's marked-to-market losses, by themselves, indicated the recommendation was not suitable for anyone.

The Hearing Panel finds that, as with other investments, the suitability of the Fund for any given customer depended on the customer's other security holdings and financial situation and needs. It is clear, however, that the Fund could only have been suitable for customers who fully understood and were willing and able to accept the risk of losing their entire investment.

It is undisputed that MHC and SW had substantial assets and large annual incomes and that their investments in the Fund constituted only a small portion of their overall investment portfolios. Therefore, both could afford to be aggressive with a portion of their portfolios, including accepting the risk of loss. It appears that SW knew that the Fund was an aggressive, risky investment, and it is undisputed that SW invested in writing put options before he invested in the Fund. Accordingly, Respondent provided evidence that he had a reasonable basis to believe that the Fund was consistent with SW's risk tolerance and investment objectives. The Hearing Panel finds that Enforcement failed to prove by a preponderance of the evidence that Respondent's Fund recommendation was unsuitable for SW.

However, Respondent had no reasonable basis for believing that the Fund was suitable for MHC, based on MHC's apparent risk tolerance. Respondent solicited DC to invest in the Fund by rolling over two of MHC's annuities, clearly much more conservative investments, yet his presentation regarding the Fund—which employed a risky and complex investment strategy and would require a detailed comprehensive explanation—took only 15 minutes. DC testified credibly that under these circumstances he did not realize that he was investing in writing put options, but rather was led to believe that he was investing in annuities with investment strategies similar to the annuities he intended to rollover into the Fund.

Respondent contended that MHC's prior investments demonstrated MHC's interest in investing in highly risky transactions. But none of those investments was as risky as the put option strategy of the Summit Fund. DC testified that the investment objective on the AGL subscription agreement was incorrectly listed as aggressive. Moreover, Respondent presented no evidence that he gathered any information from DC regarding MHC's investment objectives or risk tolerance prior to making the recommendation that MHC invest in the Summit Fund, in spite of the fact that Respondent knew that MHC was rolling over much more conservative investments into the Fund.

Accordingly, the Hearing Panel finds that Respondent did not have a reasonable basis for believing that his recommendation that MHC invest in the Fund was suitable, and thus he violated NASD Conduct Rule 2310. By violating that Rule, Respondent also violated NASD Conduct Rule 2110.

E. Count Three: Respondent Participated in Private Securities Transactions without Providing the Required Notice

Count three of the Complaint alleges that Respondent participated in the transactions with customers MHC and SW in violation of NASD Conduct Rule 3040, which requires that an associated person who intends to participate in a private securities transaction, in any manner, prior to the transaction, "provide written notice to the member with which he is associated describing in detail the proposed transaction and the person's proposed role therein and stating whether he has received or may receive selling compensation in connection with the transaction . . . ."[43]

Respondent's solicitation of customers SW and MHC to invest in the Fund and Respondent's subsequent facilitation of SW's and MHC's investments in the Fund constituted participation in a securities transaction and triggered the requirement that he notify Brookstreet in writing prior to participating in the transactions. A failure to provide required prior written notice violates Conduct Rule 3040,[44] and a violation of Conduct Rule 3040 is also a violation of Conduct Rule 2110's requirement to "observe high standards of commercial honor and just and equitable principles of trade."[45]

Respondent claimed that he did not become aware that he was registered with Brookstreet until some time after May 2, 2000. But Respondent signed a Form U-4 on April 10, 2000, and

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[43] In addition, Rule 3040 provides that, if the associated person has received or may receive compensation, the member firm must approve or disapprove of the proposed transaction in writing. If the member approves a person's participation in the proposed transaction, the transaction must be recorded on the books and records of the member and the member must supervise the person's participation in the transaction.

[44] See Stephen J. Gluckman, 1999 SEC LEXIS 1395, at **14-15 (July 20, 1999).

[45] District Bus. Conduct Comm. v. Norman M. Merz, No. C8A960094, 1998 NASD Discip. LEXIS 40 (NAC Nov. 11, 1998).

pursuant to Article I, Section (dd) of NASD's By-Laws, he thereby became associated with Brookstreet, and immediately subject to Rule 3040.[46] This was prior to Respondent's participation in the SW and MHC investments.

Furthermore, Respondent continued to participate in the transactions even after he acknowledged knowing that he was associated with Brookstreet. Respondent participated in the MHC transaction by instructing Mr. Derakshani to send DC the paperwork for the AGL annuity, and, in July 2000, Respondent participated in the SW transaction by facilitating the transfer of funds from Brookstreet to Summit Fund. Respondent's prior action, resigning from National Planning to solicit investments in the Fund, indicates his awareness of the requirements of Conduct Rule 3040. The Hearing Panel finds that Respondent actively participated in the Fund from before February 2000 through July 2000, when the last investment was made in the Fund.

The Hearing Panel finds that Respondent, while associated with an NASD member, participated in the sale of securities to customers SW and MHC without providing prior written notice of these transactions to Brookstreet, and thereby violated NASD Conduct Rules 3040 and 2110.

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[46] Respondent first met the definition of an associated person and became subject to Rule 3040 when he executed the Form U-4 on April 10, 2000. Accordingly, April 10, 2000 was the significant date for purposes of Rule 3040 rather than: (i) April 13, 2000, when NASD approved Respondent's registration with Brookstreet as a general securities representative; (ii) the first week of May 2000 when Mr. Brooks welcomed Respondent to Brookstreet; or (iii) May 24, 2000, when Respondent executed his first transaction at Brookstreet. (CX-1, p. 4; JX-11, p 1; Tr. pp. 126, 138). As a matter of law, Respondent is presumed to know and understand the NASD Rules. Carter v. SEC, 726 F.2d, 472, 474 (9th Cir. 1983).

III. SANCTIONS

A. Respondent Committed Fraud

For intentional or reckless misrepresentations or material omissions of fact, the NASD Sanction Guidelines recommend fines ranging from $10,000 to $100,000, suspensions of 10 business days to two years, and, in egregious cases, a bar.[47] In addition, a fine may be increased by the amount of the respondent's financial benefit.[48]

Enforcement argued and the Hearing Panel agreed that Respondent's commission of fraud by intentionally failing to disclose the financial performance of the Fund to customers SW and MHC was egregious and warranted a bar.[49]

The Hearing Panel finds his actions egregious for four reasons. First, Respondent deliberately failed to advise customers SW and MHC of the Fund's financial performance. Second, Respondent failed to accept responsibility for or acknowledge his misconduct; Respondent continues to fail to understand that the Fund's negative market performance was material information that any investor would have wanted to have in order to make an informed investment decision.

Third, Respondent falsely denied that he knew the Fund's negative financial condition before he solicited SW and MHC to invest monies in the Fund. The Hearing Panel does not find it credible that Respondent was ignorant of the Fund's financial condition, because: (i) his family had invested $1.7 million in the Fund; (ii) he participated in the formation and paid half of the expenses of the Fund; (iii) he routinely discussed the Fund with Mr. Derakshani; (iv) he

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[47] <u>NASD Sanction Guidelines</u>, p. 93 (2005).

[48] <u>Id.</u> at 5.

knew that the stock market was down; and (v) he had lost money on his own parallel options trading.

Finally, because of Respondent's misconduct, customers SW and MHC suffered significant financial losses. Although customers SW and MHC reached a settlement with Respondent, SW and MHC did not recoup their entire investments, and Respondent's actions required the customers to file arbitration proceedings in order to recoup some of their losses.

B. Respondent Made an Unsuitable Recommendation

For unsuitable recommendations, the NASD Sanction Guidelines suggest a fine of $2,500 to $75,000, suspensions of 10 business days to two years, and, in egregious cases, a bar.[50]

Finding that Respondent's recommendation of the Fund to DC, on behalf of MHC, was egregious, the Hearing Panel finds that Respondent's conduct warrants a bar. Respondent knew that DC believed that MHC would be investing in an annuity that invested in NASDAQ stocks, rather than in a put option strategy. The Hearing Panel finds Respondent's actions particularly egregious because Respondent solicited DC knowing that DC would simply rely on Respondent's description of the investment as an annuity similar to the type of annuities, in which MHC was already invested. The Hearing Panel also finds that Respondent testified falsely when he stated that he explained the put option strategy to DC, and that DC understood and agreed to the strategy.

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[49] Enforcement also recommended that customers SW and MHC be reimbursed; the Hearing Panel decided not to reimburse the customers in light of the settlements that were reached with Respondent.

[50] NASD Sanction Guidelines, p. 99 (2005).

C. Respondent Engaged in Private Securities Transactions

The NASD Sanction Guidelines relating to a private securities transaction recommend a fine of $5,000 to $50,000, recommend the adjudicator consider suspending the respondent for up to two years, and, in egregious cases, consider barring the respondent.[51]

Pursuant to the Guideline, the first step in determining sanctions is to assess the extent of the selling away. The following range of sanctions is suggested based on the dollar amount of sales:

Up to $100,000 in sales: 10 business days to 3 months
$100,000 to $500,000: 3 to 6 months
$500,000 to $1,000,000: 6 to 12 months
Over 1,000,000: 12 months to a bar.[52]

Following the extent of the selling away assessment, the adjudicator considers other factors as described in the principal considerations for this Guideline and the general principles applicable to all Guidelines.[53]

In determining what sanctions should be imposed in this case, the Hearing Panel considered that SW and MHC's private securities transactions involved approximately $650,000, which would warrant a suspension of 6 to 12 months.

The Hearing Panel then considered whether the sanction should be mitigated or increased by taking into account the following twelve principal considerations for this Guideline: (1) the number of customers; (2) the length of time over which the selling away activity occurred; (3) whether the product sold away has been found to involve a violation of federal or state securities

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[51] NASD Sanction Guidelines, pp. 15-16 (2005).

[52] Id.

[53] Id.

laws or federal, state or SRO rules; (4) whether the respondent had a proprietary or beneficial interest in, or was otherwise affiliated with, the selling enterprise or issuer and, if so, whether respondent disclosed this information to his or her customers; (5) whether respondent attempted to create the impression that his or her employer (member firm) sanctioned the activity, for example, by using the employer's premises, facilities, name, and/or goodwill for the selling away activity or by selling a product similar to the products that the employer (member firm) sells; (6) whether the respondent's selling away activity resulted, either directly or indirectly, in injury to the investing public, and, if so, the nature and extent of the injury; (7) whether respondent sold away to customers of his or her employer (member firm); (8) whether respondent provided his or her employer firm with verbal notice of the details of the proposed transaction and, if so, the firm's verbal or written response, if any; (9) whether respondent sold away after being instructed by his or her firm not to sell the type of the product involved or to discontinue selling the specific product involved in the case; (10) whether respondent participated in the sale by referring customers or selling the product directly to customers; (11) whether respondent recruited other registered individuals to sell the product; and (12) whether respondent misled his or her employer (member firm) about the existence of the selling away activity or otherwise concealed the selling away activity from the firm.[54]

After reviewing each of the principal considerations for this Guideline, the Hearing Panel determines that there were eight aggravating principal factors that outweighed four mitigating principal factors and one ordinarily mitigating general factor. The four mitigating principal factors were as follows: (1) there were only two customers involved; (2) the transactions

[54] Id.

occurred over a relatively short period of time; (3) there was no evidence that Respondent attempted to create the impression that Brookstreet approved the transaction; and (4) Respondent did not recruit other registered representatives to sell the Fund. Ordinarily, a member's approval of a private securities transaction in response to the representative's prior verbal notice of the private transaction would be considered a general mitigating factor for the representative's failure to provide prior written notice. In this case, however, in the absence of Respondent's providing prior verbal notice of his intention, the Hearing Panel does not consider Brookstreet's subsequent approval of the transaction mitigating.

The Hearing Panel particularly noted the following four aggravating principal factors: (1) Respondent participated in the selling away after Brookstreet warned him about such activity; (2) Brookstreet incurred actual damages as a result of Respondent's conduct; (3) Respondent's selling away resulted in harm to his customers; and (4) the selling away involved violations of the securities laws and SRO rules, i.e., fraud and unsuitability.

The Hearing Panel also noted the following four additional aggravating principal factors: (1) Respondent had an expectation and ability to acquire a proprietary interest in the issuer through its general partner Summit Management; (2) SW was a customer of Respondent's employer; (3) Respondent provided verbal information concerning the SW transaction only after another Brookstreet employee alerted management of the proposed wire transfer; and (4) Respondent sold the Fund directly to the customers.

Finally, the Hearing Panel considered as a particularly aggravating general factor that Respondent, if not intentionally, recklessly engaged in the private securities transactions, rather than negligently engaged in them. Knowing that there was a Conduct Rule 3040 issue, Respondent took no steps to insure that he was in compliance with the Rule.

The Hearing Panel finds that these aggravating factors even when counterbalanced by the mitigating factors demonstrate that Respondent's misconduct was egregious and warrants a bar. Accordingly, the Hearing Panel, consistent with the Guideline, bars Respondent from association with any NASD member.

IV. CONCLUSION

Respondent Dana N. Frankfort is barred for violating: (i) Section 10(b) of the Exchange Act, SEC Rule 10b-5 thereunder, and Conduct Rules 2120 and 2110; (ii) Conduct Rules 2310 and 2110; and (iii) Conduct Rules 3040 and 2110, as alleged in counts one, two, and three of the Complaint. The bars shall become effective immediately upon this Decision becoming the final disciplinary action of NASD.[55]

HEARING PANEL

____
Sharon Witherspoon
Hearing Officer

Dated: Washington, DC
February 1, 2006

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[55] The Hearing Panel 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.