BEFORE THE NATIONAL ADJUDICATORY COUNCIL

NASD REGULATION, INC.

In the Matter of The Department of Enforcement, Complainant, vs. Michael Galasso, Jr. Staten Island, NY, Gerard McMahon Belford, NJ, John Montelbano New York, NY, Dwayne Leverett Hackensack, NJ, Todd Nejaime Plantation, FL, Respondents.	AMENDED DECISION Complaint No. C10970145 Dated: February 5, 2001

Michael Galasso ("Galasso"), John Montelbano ("Montelbano"), and Gerard McMahon ("McMahon") appealed a December 10, 1999 Hearing Panel decision pursuant to Procedural Rule 9310. We called this matter for review to examine the findings and sanctions as to Dwayne Leverett ("Leverett") and Todd Nejaime ("Nejaime"). We affirm the Hearing Panel's findings in part and modify them in part, and modify the sanctions imposed by the Hearing Panel.[1]

[1] A summary of the NAC's findings and sanctions as to each of these respondents is set forth at

I. Background

Monitor Investment Group, Inc. ("Monitor" or "Firm") was a member of the NASD from August 1992 until October 21, 1996, when it filed a Broker-Dealer Withdrawal Form ("Form BDW") with the NASD. On January 23, 1998, the Department of Enforcement ("Enforcement") filed a complaint against Monitor and 17 individual respondents alleging participation in a scheme to manipulate the price and supply of Accessible Software, Inc. ("ASWI") shares, which resulted in fraudulent and excessive mark-ups to Monitor customers who had purchased ASWI shares on May 13-14, 1996.[2]

Prior to or at the time of the hearing below, 10 respondents were held in default by the Hearing Officer who presided over the proceedings below.[3] The remaining eight respondents appeared at the hearing and contested the allegations. Those eight respondents, all employed by Monitor, were Galasso (trader), McMahon (held the title of research analyst but had a broader role than his title would suggest), Montelbano (Monitor's acting president during the relevant period), Leverett (registered representative and general securities principal), Nejaime (registered representative), Emmanuel Gennuso ("Gennuso") (Monitor operations and compliance officer), Patrick Giglio ("Giglio") (registered representative), and Steven Goldstein ("Goldstein") (registered representative). Only Galasso, McMahon, Montelbano, Leverett and Nejaime are the subject of this review.

During the relevant period, Monitor had offices in three different locations in New York City: 20 Exchange Place; 30 Broad Street; and 919 Third Avenue.[4] Galasso, Leverett, and Nejaime all worked out of the Third Avenue office, which is where Monitor's trading operation was located. McMahon and Montelbano worked out of the Broad Street office, which was considered to be Monitor's headquarters.

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the conclusion of this decision. See pp. 43-48.

[2] An amended complaint was filed on October 15, 1998 to correct certain typographical errors.

[3] The Office of Hearing Officers issued a default decision as to the 10 defaulting respondents on October 27, 2000. Although Monitor and these individuals defaulted by their failure to participate in the disciplinary proceeding below, we refer to three of the defaulting respondents in this decision because of their prominent roles in the management of Monitor. These individuals are: William Palla ("Palla") (one of the apparent owners of the Firm, who was previously barred by the NASD for failing to respond to the staff's inquiries into the Monitor scheme), Jeffrey Pokross ("Pokross") (an individual who appeared to have a controlling interest in the Firm), and Salvatore Piazza ("Piazza") (an individual who appeared to have a controlling interest in the Firm).

[4] For purposes of this matter, only the Third Avenue and Broad Street offices are relevant to our discussion of the allegations at issue.

Galasso, the Firm's trader, was associated with Monitor from November 1994 to July 1996 and worked out of the Third Avenue office. He was registered as a general securities representative and options principal at the Firm during the relevant period (May 1996). Although the Central Registration Depository ("CRD") lists Galasso's position at Monitor during the relevant period as "OTC Operator," the evidence shows that he was Monitor's sole trader during that period. Galasso, as Monitor's sole trader, was charged, among other things, with knowingly and/or recklessly manipulating the price and supply of ASWI on May 13-14, 1996.

McMahon was Monitor's research analyst but, in fact, had a broader role at Monitor than his title would suggest. In the regular course of his duties at Monitor, he reviewed prospective business deals that were presented to him by Pokross and he conferred with Palla regarding Monitor's market-making activity. He worked out of Monitor's Broad Street office but had contact with brokers from both Broad Street and Third Avenue. McMahon was associated with Monitor from September 1995 through August 1996 as a general securities representative. The complaint alleged that McMahon knowingly engaged in activities with the intent artificially to condition the market for ASWI and facilitate the distribution of shares of ASWI to Monitor customers at a pre-determined price. The complaint further alleged that McMahon encouraged Monitor brokers to utilize high-pressure sales tactics, including the use of misrepresentations and price predictions without any reasonable basis in the marketing of ASWI to Monitor customers.

Montelbano was acting as Monitor's president during the relevant period. He worked out of Monitor's Broad Street office and was associated with Monitor from September 1995 to August 1996. The complaint alleged that Montelbano knowingly engaged in activities with the intent to and the result of, artificially conditioning the market to facilitate the distribution of shares of ASWI to Monitor customers at a pre-determined price. The complaint also alleged that Montelbano encouraged Monitor brokers to utilize high-pressure sales tactics, including the use of misrepresentations and price predictions without any reasonable basis in the marketing of ASWI to Monitor customers.

Leverett was a principal at the Third Avenue and was responsible for reviewing and approving order tickets when Palla was not in the office. Leverett was associated with Monitor from February to May 1996. He was alleged to have been involved in the ASWI scheme by engaging in manipulative and deceptive sales practices in connection with his sales of ASWI to two customers and by reviewing and approving falsified order tickets in connection with the ASWI trades that occurred on May 13-14, 1996. Leverett also was charged with failure to supervise for the regulatory abuses that were alleged to have occurred at Monitor in connection with the manipulation of the price and supply of ASWI shares. He had been a principal at Monitor for approximately six days when the manipulation of ASWI shares occurred.

Nejaime was an assistant to Palla and worked at Monitor's Third Avenue office. He was associated with Monitor from January to July 1996, but did not become registered as a general

securities representative with the Firm until April 8, 1996. Nejaime assisted Palla primarily by recruiting brokers to work at Monitor during the relevant period.[5] The complaint alleged, among other things, that he engaged in manipulative and deceptive sales practices by coordinating the allocation of ASWI shares to Monitor brokers.

II. Facts, Findings and Conclusions

A. The ASWI Manipulation

1. Monitor's ASWI Sales Campaign

Monitor conducted a major sales campaign prior to May 13, 1996, the date that Monitor began trading ASWI shares, to mobilize its sales force to sell shares in ASWI to its retail customers. McMahon and Montelbano gave Monitor brokers misleading information about ASWI that was designed to give them the impression that ASWI was a good investment for Monitor retail customers, even though the company's financial information showed that it had operated historically at a deficit.[6] Monitor brokers were advised on May 13, 1996 to start selling ASWI shares to their customers. Brokers testified that they were told that ASWI was a "new issue," that it would be an initial public offering ("IPO"), or that it would be a private placement under Exchange Act Rule 504 of Regulation D ("Rule 504"). In fact, the shares that Monitor brokers sold to retail customers on May 13 and 14, 1996, were not offered in connection with either an IPO or a private placement. ASWI started trading on the over-the-counter ("OTC") Bulletin Board ("OTCBB") on May 13, 1996, which was the same day that Monitor brokers commenced selling ASWI shares to retail customers.[7] The Hearing Panel found that McMahon and Montelbano told Monitor brokers: (1) that the Firm only had a certain number of shares to allocate; (2) that they would receive a sales credit in connection with the sale of shares of ASWI; and (3) the price at which ASWI would be sold when it started trading.

2. The Rule 504 Offering of ASWI

The record demonstrates that Palla, Pokross, Piazza, and James Labate ("Labate") (who was not charged with any misconduct in this proceeding) were owners, controlling persons, or partners in the

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[5] Although the complaint alleged that Nejaime was a "manager," there is no evidence that Nejaime, in fact, was acting in the capacity of a "manager."

[6] ASWI had been incorporated in 1995 and was a company whose primary business was the development of "multi-platform systems management" software programs.

[7] The OTCBB is a quotation medium that publishes bid and asked quotations of over-the-counter stocks not meeting the minimum-net worth and other listing and maintenance requirements of the Nasdaq Stock Market.

ownership or control of Monitor. During the period December 1995 through March 1996, entities controlled by, or persons related to, Piazza and/or Pokross and their associate, Labate, purchased ASWI at $1 per share pursuant to a Rule 504 offering. Monitor affiliates or controlling persons of Monitor, through relatives and associates, had acquired 485,000 shares out of the 535,000 shares that were available through the Rule 504 offering. Labate and Pokross transferred 125,000 of these 485,000 shares to NASD member firm Baird Patrick & Co., Inc. ("Baird Patrick") prior to the commencement of trading on May 13-14, 1996, for the account of DMN Capital Investment, Inc. ("DMN"), an entity that was controlled by Labate and Pokross.

3. Monitor's Manipulation of Trading in ASWI Shares on May 13-14, 1996

On May 10, 1996, Monitor received authorization from the NASD to make a market in ASWI. The forms that Monitor had filed previously with NASD Regulation pursuant to SEC Rule 15c2-11 ("Forms 211") in order to initiate quotations in ASWI disclosed that the initial bid and ask prices would be $0.875 and $1.25, respectively, and that the price had been determined by reference to a Rule 504 private placement of $1 per share. On May 13, 1996, Monitor, the sole market maker in AWSI, acting through Galasso, posted at 10:26 a.m. initial bid and ask prices of $0.875 and $1.25.

The Hearing Panel found that Galasso, Monitor's only trader, allocated shares of ASWI to customers' orders at predetermined prices with predetermined special compensation to Monitor brokers in the form of sales credits, having no relationship to market forces. On May 13, 1996, Galasso moved the price of ASWI from $1.25 to $9.375 in less than two hours by means of a series of 12 inter-dealer transactions. The Hearing Panel found that, shortly after having up-ticked the price of ASWI, Galasso proceeded to move the price of ASWI downward through a series of purchases from the DMN account at Baird Patrick so that he could execute the customer orders at the predetermined prices indicated on the May 13, 1996 tickets and give the brokers the $2.25 sales credit that was reflected on the order tickets.

The Hearing Panel found that McMahon and Montelbano engaged in manipulative and deceptive acts in connection with the purchase and sale of ASWI by touting ASWI to Monitor brokers as a good investment prior to the commencement of trading on May 13, 1996. The Hearing Panel found that Montelbano and McMahon gave Monitor brokers misleading information about ASWI in an effort to mobilize the Monitor sales force to sell ASWI at predetermined prices and promised large predetermined credits to the brokers.

a. Legal Standards. Manipulation is a "term of art . . . connot[ing] intentional or willful conduct designed to deceive or defraud investors by controlling or artificially affecting the price of securities." Ernst & Ernst v. Hochfelder, 425 U.S. 185, 199 (1976). The Securities and Exchange Commission ("Commission" or "SEC") has stated that:

> In essence, a manipulation is intentional interference with the free forces of supply and demand. Proof of a manipulation almost always depends on inferences drawn from a mass of factual detail. Findings must be gleaned from patterns of behavior, from apparent irregularities, and from trading data. When all of these are considered together, they can emerge as ingredients in a manipulative scheme designed to tamper with free market forces.

In re Pagel, Inc., 48 S.E.C. 223, 226 (August 1, 1985), aff'd sub nom. Pagel, Inc v. SEC, 803 F.2d 942 (8th Cir. 1986). Manipulation has also been defined as the deceptive movement of a security's price accomplished by an intentional interference with the forces of supply and demand. In re Patten Securities Corp., 51 S.E.C. 568, 572 (1993) (citing Ernst & Ernst, supra, at 199); Pagel, Inc. at 226. Section 10(b) of the Securities and Exchange Act of 1934 ("Exchange Act") prohibits any manipulative or deceptive device in connection with the purchase or sale of any security and Rule 10b-5 thereunder prohibits any device, scheme, or artifice to defraud in connection with the purchase or sale of any security.

In the present case, we find many of the "classic earmarks" of a manipulation, as described in more detail below: a rapid price surge dictated by Monitor, the firm that controlled the market in ASWI; little investor interest; an abundant supply of ASWI shares from the DMN account at Baird Patrick; and the absence of any known prospects for ASWI or favorable developments affecting it.[8]

The complaint alleged that Galasso, McMahon and Montelbano violated Exchange Act Section 10(b) and Rule 10b-5, Conduct Rule 2110, as well as Conduct Rule 2120 (causes seven, five, and four respectively). In order to establish liability under Exchange Act Section 10(b), Rule 10b-5 and Conduct Rule 2120, we must find not only that the respondents participated in the manipulation but also that they acted with "scienter." Scienter is a "mental state embracing intent to deceive, manipulate, or defraud." Ernst & Ernst, supra at 193, n.12. Scienter is often established by circumstantial evidence. In re Meyer Blinder, 50 S.E.C. 1215, 1229-30 (1992); see also In re Blech Securities Litigation, 961 F.Supp. 569, 582 (S.D.N.Y. 1997) (scienter can be inferred from circumstantial evidence). Scienter can also be established by proving that the respondent acted with recklessness. In re Meyer Blinder, supra.[9] Recklessness has been defined as "an extreme departure from the standards of ordinary care . .

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[8] See In re Patten, supra; In re Jay Michael Fertman, 51 S.E.C. 943 (1994); See also In re Pagel, supra, at 226; Edward J. Mawod & Co. v. SEC, 591 F.2d 588, 591 (10th Cir. 1979); SEC v. Resch-Cassin & Co., 362 F. Supp. 964, 976-77 (S.D.N.Y. 1973); Dlugash v. SEC, 373 F.2d 107, 109 (2d Cir. 1967).

[9] The Supreme Court has expressly reserved the issue of whether "recklessness" is sufficient to prove scienter under Rule 10b-5. See Ernst & Ernst, supra at 193 n. 12. Most Circuit Courts of Appeal, however, have held that "recklessness" satisfies the Rule 10b-5 scienter requirements. Louis

. which presents a danger of misleading buyers or sellers that is either known to the defendant or is so obvious that the actor must have been aware of it."[10] We will discuss Galasso's, McMahon's, and Montelbano's roles in the manipulation separately below.

b. Galasso Participated in the Manipulation of ASWI Shares. In the first stage of the manipulative trading on May 13, 1996, Galasso up-ticked the price of ASWI from $1.25 to $9.375 in slightly under two hours, by means of 12 inter-dealer trades.[11] The customers who purchased ASWI shares through those inter-dealer trades all had connections to Monitor. Galasso's first inter-dealer trade on May 13, 1996 was a sale of ASWI to Monarch Financial ("Monarch") for the account of his grandparents. Galasso's subsequent inter-dealer sales were to: (1) Ernst & Co. ("Ernst") for the account of Astaire & Partners, whose Monitor account was serviced by McMahon and Montelbano; and (2) Dean Witter for the account of John Serpico, whose Monitor account was serviced by Giglio, another respondent named in the complaint.

Galasso began trading ASWI shares on May 13, 1996 without an inventory. He took a short position in 10 out of the 12 inter-dealer transactions he effected on May 13, 1996 and was "flat" (with neither a long or short position) in two of the transactions. From 10:29 a.m. to 12:25 p.m., Galasso moved the price of ASWI upwards through a pattern that included: (1) ever-escalating quotes (starting at $.875 bid and $1.25 asked at 10:26 a.m. and increasing incrementally to $6 bid and $9.375 asked by 12:24 p.m.); (2) 12 inter-dealer sales that started at 10:29 a.m. at a price of $1.25 and ended at 12:25 p.m. at a price of $9.375 (for a total of 7,000 shares, with transactions ranging in increments from

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Loss & Joel Seligman, Securities Regulation, Vol. VIII, ch.9, 'B(6), at 3665-67 n. 521 (3d ed. 1991) (11 circuits have held that showing of recklessness is sufficient to prove scienter).

[10] Scienter is also required under Rule 2120, and it may be satisfied by a showing of intentional or reckless conduct. In re Kevin Eric Shaughnessy, Exchange Act Rel. No. 40244 (Jul. 22, 1998).

[11] One of those 12 interdealer trades was a completely sham transaction. On May 13, 1996, at 12:05 p.m., Galasso reported to the NASD tape a sale of 1,000 shares to Ernst at a price of $4.25. Although Galasso canceled the trade with Monitor's clearing firm, he failed to report the transaction as a canceled trade to the NASD until several days later. The Ernst trader, Anne Magelinsky ("Magelinsky"), testified at hearing that she had never placed that particular order with Galasso. Just prior to the sham transaction, Monitor's bid and ask prices were $2.375 and $5.375, respectively, and Galasso had purchased 1,000 shares from the Baird Patrick DMN account at $2.375. Approximately one minute and 20 seconds prior to placing the sham transaction, Galasso posted bid and ask prices of $3 and $5.375, respectively. Then, approximately one and one-half minutes after having placed the sham transaction as a sale to Ernst at a price of $4.25, Galasso sold 500 shares to Dean Witter at a price of $5.375. Thus, as the Hearing Panel noted, the net effect of this sham transaction was to facilitate the movement of ASWI's price from $2.375 to $5.375.

500 to 2,000 shares); and (3) three purchases of ASWI shares from the DMN account at Baird at 10:53 a.m. (2,000 shares), 11:15 a.m. (1,000 shares), and 11:56 a.m. (1,000 shares) (for a total of 4,000 shares) at successively higher prices. William Shields, one of the NASD examiners who investigated Monitor's activities during the relevant period, testified that this series of up-ticks in the price of ASWI was unrelated to any available news relating to ASWI or any sudden market demand in shares of ASWI.

Galasso was also involved in a second stage of manipulative trading: Less than an hour after having moved the price of the shares to $9.375, he began moving the price of ASWI downward through a series of 10 transactions involving the DMN account at Baird Patrick. The record shows that, at the time Galasso was moving the price of ASWI downward, Monitor had a short position and needed cheap inventory to fill retail customer orders at predetermined prices that took into account predetermined sales credits that had been promised to the sales force. Galasso purchased into inventory 89,500 shares of ASWI between 3:37 p.m. and 4:13 p.m. from the DMN account at Baird Patrick at ever-decreasing prices from $6.75 to $3.875. Galasso testified at hearing that he followed Palla's instructions and had moved the price of the stock downward to achieve a differential between the inventory price and the retail sale price that was large enough to accommodate the $2.25 per share sale credit that was included on the majority of the original trade tickets that were executed on May 13, 1996.[12]

John D'Angelo ("D'Angelo"), the trader who effected the ASWI transactions at Baird Patrick, testified that Pokross (one of the individuals who appeared to have a controlling interest in Monitor and who was one of the joint account holders of the DMN account) called him at certain intervals on May 13, 1996 and each time directed him to sell a certain number of ASWI shares from the DMN account. D'Angelo testified that Pokross directed him to sell ASWI at intervals throughout the day on May 13 to Monitor (which were executed through Galasso) because Monitor was the only market maker in ASWI during the relevant period. Galasso admitted during his on-the-record interview that he had an arrangement with the Baird Patrick trader to supply ASWI shares.[13] Although Galasso denied having such an arrangement at hearing, we credit his on-the-record admission which was used by Enforcement to impeach his hearing testimony. On the basis of the foregoing evidence, which is corroborated by the documentation establishing the course of dealing, we conclude that Galasso knew that he would be able to move the price of ASWI downward because he had an arrangement with Baird Patrick to supply ASWI shares to Monitor during the relevant period.

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[12] Galasso obtained 66,000 out of the 89,500 shares at ever-decreasing prices ranging from $4.375 to $3.875 per share, and he effected most of the retail sales at a price of $6.75, thus allowing for the $2.25 per share sales credit.

[13] When Galasso was asked at hearing if the arrangement was between him and D'Angelo, he testified that it was with "Johnny D." D'Angelo confirmed in his hearing testimony that he was referred to as "Johnny D."

After obtaining the inventory he needed to fill retail orders, Galasso allocated the ASWI shares in his inventory to customer accounts at the end of the day on May 13, 1996.[14] He then executed the customer orders between 4:16 p.m. and 6:13 p.m. on May 13, 1996 at predetermined prices (e.g., more than 42 customer orders from brokers at the Third Avenue office were executed at a uniform price of $6.75) and with predetermined sales credits (the majority at $2.25).[15] When Galasso ran out of shares to allocate to approximately 30 customer orders, instead of executing the orders and taking a short position, the tickets were marked with the designation "ND," which stood for "not done."[16]

Galasso executed the "not done" orders the next day, on May 14, 1996. In order to effect the "not done" transactions from the previous day, Galasso purchased more shares of ASWI on May 14, 1996 from the DMN account at Baird Patrick at a price of $5. He then executed the majority of the "not done" orders from May 14, 1996 at the predetermined price of $6.375 per share, and with predetermined credits to the brokers ranging from $1 to $1.25 per share.[17]

The Hearing Panel found that Monitor dominated and controlled the market for ASWI shares on May 13-14, 1996 to such an extent that there was no independent competitive market for the ASWI shares, and Monitor controlled the wholesale prices.[18] Monitor was the only market maker in ASWI

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[14] Galasso testified at hearing that he received a stack of ASWI order tickets at the end of the day on May 13, 1996 and that he then proceeded to allocate shares in his inventory to customer accounts. Galasso described ASWI as a "new issue" and admitted that he had treated the shares as if they were shares in an IPO. Some of the Monitor brokers also described ASWI as a "new issue."

[15] The order tickets -- with the limit, execution, and reported prices all at the same price -- provide documentary evidence that the prices were predetermined. Galasso also testified that the price at which ASWI would trade and the sales credits that the brokers were to receive in connection with the sales of ASWI shares were both predetermined prior to the commencement of trading on May 13, 1996. Leverett, a co-respondent in this matter, corroborated Galasso's testimony regarding the predetermined sales credits. See, infra, note 50.

[16] The majority of those tickets came from the Broad Street office. There is conflicting evidence as to whether the tickets were sent from the Broad Street office with the "ND" designation or whether the designation was entered by someone in the trading room.

[17] The record shows that Galasso entered quotes for ASWI on May 14, 1996 that had no relation to market forces (starting at $4.75 bid and $7.875 at 9:39 a.m. and increasing to $5.75 bid and $8.75 asked at 11:43 a.m.). Like the order tickets that were executed on May 13, 1996, the tickets that were executed on May 14, 1996 also bore identical limit, execution, and reported prices.

[18] See In re Steven B. Theys, 51 S.E.C. 473 (1993); In re Michael Alan Leeds, 51 S.E.C. 500, 503 (1993); In re Meyer Blinder, 50 S.E.C. 1215 (1992).

during the relevant period and there was virtually no inter-dealer trading away from Monitor during the relevant period. As discussed above, the inter-dealer trades that Monitor made were with broker-dealers that were trading for accounts that were controlled by individuals who had a connection to Monitor in some manner. Monitor purchased 23% of the public float in ASWI stock from the DMN account between May 13 and 14, 1996[19] (which represented 94.67% of all ASWI shares purchased on those dates) and sold 90% of those shares to its retail customers. Monitor was involved in one side or the other in 100% of the ASWI trades that occurred on those dates.

We find that Galasso knowingly manipulated the price of ASWI. Galasso participated in the fraudulent scheme by effecting the very buy and sell orders that artificially manipulated ASWI's stock price upward and downward. See SEC v. U.S. Environmental, 155 F.3d 107 (2d Cir. 1998). The evidence demonstrates that Galasso: (1) knew about the $1 share price of ASWI from the previous Rule 504 offering; (2) engaged in 12 pre-arranged[20] inter-dealer transactions to up-tick the price of ASWI and then, because he had a short position, proceeded to down-tick the price of ASWI in order to obtain ASWI shares at prices that would allow customer orders to be executed with predetermined prices and sale credits; and (3) executed customer orders on May 13-14, 1996 at prices having no relation to market forces. All of these factors demonstrate that Galasso played a central role in the manipulation of ASWI shares and contributed to the distortion of the market for ASWI shares and the creation of a "stagemanaged performance." See Edward J. Mawod & Co., 46 S.E.C. 865 (1977), aff'd, Mawod, supra (quoting In re Halsley, Stuart & Co., Inc., 30 S.E.C. 106 (1949)). We therefore also find more than sufficient evidence of scienter on the part of Galasso and thus affirm the Hearing Panel's findings of violation as to Section 10(b), Rule 10b-5, and Conduct Rules 2110 and 2120.

Galasso did not deny that any of the above-described trading occurred. Instead, he attempted to shift the blame to others and argued that he lacked information about the transactions.[21]

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[19] The Hearing Panel found that Baird Patrick had sold Monitor "24%" of the publicly tradable float of ASWI shares. Our calculation regarding the percentage of the public float obtained by Monitor differs slightly from that of the Hearing Panel. There were 535,000 ASWI shares offered through the Rule 504 offering, 485,000 of which were acquired by Monitor affiliates or controlling persons of Monitor. After Monitor controlling persons transferred 125,000 ASWI shares to the DMN account at Baird Patrick, Monitor acquired 124,500 of those shares from Baird Patrick, resulting in Monitor having obtained 23% of the public float.

[20] The Hearing Panel concluded that Galasso had engaged in "pre-arranged" transactions in order to create an artificial market demand for ASWI based on evidence that the accounts that were involved in the 12 inter-dealer transactions all had a connection with Monitor. (See discussion of inter-dealer transactions above on p. 7.) We adopt this finding.

[21] Although Galasso stated in his appeal letter that it was his intent to appeal only his sanctions, we have analyzed the Hearing Panel's sanctions and findings because Galasso's arguments on appeal also challenged the Hearing Panel's findings.

First, Galasso argued throughout the proceedings below that he lacked critical information about the ASWI transactions. He testified that he was merely following the directions of Monitor's counsel when he filled out and filed the Forms 211 and that he did not understand anything about the Form 211 process. The Hearing Panel did not credit Galasso's testimony, noting that Monitor's attorneys had advised him about the meaning of the forms and had explained the concept of a Rule 504 offering to him before he signed the forms. Credibility determinations of an initial fact finder are entitled to considerable weight. See Alderman v. SEC, 104 F.3d 285 (9th Cir. 1997); In re Ashvin R. Shah, 52 S.E.C. 1100 (1996); In re Jay Houston Meadows, 52 S.E.C. 778 (1996), aff'd, Meadows v. SEC, 119 F.3d 1219 (5th Cir. 1997). We find no basis in the record to depart from the Hearing Panel's credibility determination. Galasso admitted at hearing that he knew that ASWI's price in the Rule 504 offering was $1, information that was included in the Forms 211 that he completed and filed. Thus, we fail to see the relevance of Galasso's argument that he lacked critical information about the transactions.

Second, Galasso argued that he was only following Palla's orders when he moved the price of ASWI. Even if Palla was directing the manipulative activity, however, Galasso's misconduct would not be excused. Members and associated persons are responsible for knowing and following regulatory requirements. In re Jeffrey D. Field, 51 S.E.C. 1074, 1076 (1994) (quoting In re Kirk A. Knapp, 51 S.E.C. 115, 134 (1992)) ("participants in the industry must take responsibility for their compliance with applicable regulatory requirements and cannot be excused for lack of knowledge, understanding, or appreciation of these requirements").

Third, Galasso argued that he was not at fault because he did not "write" the order tickets. We agree with the Hearing Panel that this argument has no merit.[22]

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[22] Galasso testified that when he received the order tickets, the following information was included on the tickets: the execution, reported, and limit prices and the brokers' credits. The salesmen testified that they had placed some of the information on the tickets, including the limit price, but denied that the reported and execution prices and the sales credit amounts were in their handwriting. Although there is no evidence in the record that resolves the issue of who was actually responsible for completing the order tickets, our analysis is not affected by this lack of information.

In addition, in an apparent effort to supplement his arguments on appeal, Galasso filed a request to submit additional attachments to his answering brief one business day prior to the appeal hearing in this matter. The attachments consisted of his summaries of certain on-the-record interviews and hearing transcripts and certain trade records, all of which appeared already to be contained in the record. Following argument by the parties, including Enforcement's opposition to the request, the NAC Subcommittee that heard this appeal ruled that it would not accept the additional documents into the record. We find that Galasso's request to introduce additional evidence did not satisfy the requirements of Procedural Rule 9346: (1) it was not timely filed; (2) it did not describe each item of proposed new evidence; and (3) it did not demonstrate that the evidence was material. Accordingly, we affirm the

c. McMahon Participated in the Manipulation of ASWI Shares. McMahon worked at Monitor's main office at Broad Street and had contact with brokers from both the Broad Street office and the Third Avenue office in his capacity as Monitor's research analyst. Monitor brokers from both offices testified that McMahon touted ASWI as a good investment; had given certain brokers information about the price at which ASWI would sell; and had told certain brokers that they would receive a sales credit in connection with the sale of ASWI shares. The Hearing Panel also found that McMahon had given the brokers misleading information to induce them to sell ASWI shares to their customers once trading commenced. As a preliminary matter, we address the following arguments that McMahon made about the credibility of the testimony provided by the brokers who testified against him: (1) that the Monitor brokers testified against him because they feared for their safety and loss of their NASD registrations; (2) that the testimony of certain brokers was not credible because they also were respondents in this matter and had reason to implicate McMahon, rather than themselves, in the scheme to manipulate ASWI shares; and (3) that the on-the-record testimony of certain brokers was not credible because they did not testify at the hearing, and he was not able to cross-examine them.

As to McMahon's first argument, we note that McMahon provided no evidence in these proceedings that supports his contention that Monitor brokers lied about his involvement in ASWI because they feared for their safety or for the loss of their NASD registrations. The Hearing Panel found that McMahon's contention was contradicted by the testimony of Kristian Sierp ("Sierp"), who, when asked at the hearing by Montelbano whether he feared for his safety, responded, "no, not at all." Nevertheless, we do not believe that McMahon's argument fails based solely on Sierp's testimony. Rather, we find that, as a general matter, the record contains insufficient evidence to establish that fear had anything to do with the manner in which the brokers had testified.

With respect to his second argument, McMahon asserts that Goldstein's and Nejaime's testimonies are questionable because they were also respondents in this matter and that they therefore had a motive to divert attention away from their own conduct and focus that attention on someone else. He also contends that brokers Herkert's and Telmany's testimony is questionable because they were respondents in this matter and had been held in default by the Hearing Panel for failing to appear at pre-hearing conferences. We reject McMahon's attempts to have us totally disregard the testimony of these individuals simply because they are also respondents in this matter. Although the Hearing Panel did not make specific credibility findings as to the witnesses who were also respondents in this matter, we have found these witnesses' testimony to be consistent and mutually corroborative, and thus credible. Indeed, the Hearing Panel found McMahon's argument that he had never spoken to any brokers about ASWI prior to the commencement of trading wholly contradicted by the great weight of evidence. We adopt that finding based on the evidence detailed below. As to the credibility of Herkert's and Telmany's on-the-record statements, we discuss the probative value of those statements below.

(continued)
Subcommittee's ruling.

Regarding McMahon's third argument, we note that the on-the-record testimony of brokers who did not testify at hearing is hearsay. Hearsay is admissible in NASD proceedings provided it is found to be reliable and probative. In re Michael A. Niebuhr, 52 S.E.C. 546 (1995); Richardson v. Perales, 402 U.S. 389 (1971). Unless otherwise noted in the discussion below, we find that this evidence is reliable because it satisfies a number of the factors that the Commission has identified as bearing on the reliability and probative value of hearsay evidence. Niebuhr, supra; In re Gary L. Greenberg, 50 S.E.C. 242, 245 (1990) (citing Richardson, supra). First, although some of the witnesses who provided on-the-record testimony are also respondents in this matter, we find no evidence that these individuals had any specific biases against McMahon, nor did McMahon introduce such evidence. Second, the reliability of the hearsay statements is supported by the fact that they were not contradicted by direct testimony from other brokers. Third, the hearsay at issue consists of sworn oral statements in the form of on-the-record testimony.

We turn first to the evidence that the brokers from Monitor's Third Avenue office provided about McMahon's involvement in the manipulation of ASWI shares. Five brokers testified at hearing that McMahon had conducted a sales meeting regarding ASWI approximately one week prior to the commencement of Monitor's trading activity on May 13-14, 1996, and that during that meeting he had touted the company as a very good opportunity to make money and had compared it favorably to a company called Tivoli (a company that James Tagliareni ("Tagliareni"), the president of ASWI, previously had taken public), that had been purchased by IBM for more than $700 million.[23] Brokers from the Third Avenue office also testified that McMahon had: (1) provided price projections for ASWI in the short term of $15-$20 and in the long term of $100;[24] (2) explained that there were a limited number of shares available that could be allocated to the brokers;[25] (3) said that he liked the stock so much that he was taking ASWI warrants or stock as his investment banking fee;[26] (4) told

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[23] The Third Avenue brokers who provided this information at hearing were Michael Hogan ("Hogan") and Michael Kardish ("Kardish"), and other respondents Nejaime, Leverett, and Goldstein.

[24] Brokers Hogan, Kardish, and respondent Goldstein testified at hearing about these facts.

[25] Hogan testified at hearing that he could not remember the number of shares that McMahon had said would be available but admitted that his recollection of the issue had been clearer at his on-the-record interview when he testified that McMahon had told him that there were very few shares available.

[26] Hogan testified at hearing that McMahon said that he liked the company so much that he was taking his investment banking fee in warrants rather than in cash. Goldstein testified at hearing that McMahon advised him that McMahon was offered a fee for his role in the ASWI deal but that he took stock in ASWI instead.

them that the ASWI shares were being sold as part of a Rule 504 offering;[27] and (5) told them the commission they would earn on ASWI transactions and the price at which ASWI was going to be sold.[28]

We now turn to the evidence provided by the brokers from the Broad Street office about what McMahon had told them about ASWI prior to the commencement of trading on May 13-14, 1996. Brokers from the Broad Street office testified that McMahon had: (1) told them that only a limited number of shares would be available to their customers;[29] (2) advised them that they would receive a special credit of between $5/8 and $1 per share;[30] (3) provided them with price predictions of between $20-$40 per share;[31] (4) told them the price at which ASWI was scheduled to sell;[32] (5) told them that

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[27] Goldstein testified at hearing that McMahon discussed ASWI in terms of a Rule 504 offering.

[28] Goldstein testified at hearing that McMahon had told him prior to the commencement of trading in ASWI the amount of commissions that he would earn. His testimony did not, however, reference a specific dollar amount. The documentary evidence shows that the original order tickets for the trades that came from the Third Avenue office contained a sales credit of $2.25 per share. Respondent Nejaime testified at his on-the-record interview that McMahon had told him that ASWI would be trading in the range of $6 or $7. Other brokers testified that they knew that ASWI would trade at a price of $6.75. Brokers from the Broad Street office also testified that McMahon had told them that they would be receiving a special sales credit and that ASWI would be trading at a particular price. See infra, notes 30 and 32.

[29] Sierp testified at hearing that McMahon and Montelbano had told him that they had about 10,000 to 12,000 shares of ASWI and that the brokers could place the shares with their customers. Although Telmany (one of the respondents mentioned above who defaulted in the proceedings below) initially testified that McMahon had told him he would only be allocated 4,000 shares of ASWI, we do not find Telmany's on-the-record interview on this issue to be probative because he later testified that he thought Montelbano was the person who had told him that he would only be allocated 4,000 shares of ASWI. We therefore do not accept the Hearing Panel's finding that Telmany's testimony was evidence that McMahon had told him the number of ASWI shares that would be allocated to him.

[30] Sierp testified at hearing that McMahon and Montelbano had told him that he would be receiving a credit of $5/8 to $1 per share on the ASWI tickets. Telmany testified in his on-the-record interview that McMahon and Montelbano had told him that he would earn $1 per share on the ASWI transactions.

[31] Telmany testified in his on-the-record interview that McMahon and Montelbano had said that ASWI would be a "good stock" and that it would go to $20.

[32] Telmany testified in his on-the-record interview that McMahon and Montelbano had told him that ASWI would be offered at a price of $8 or $8 1/4.

ASWI was a great trading opportunity because it was a very good company;[33] and (6) given them materials about ASWI and/or advised the brokers about the merits of ASWI and Tivoli.[34]

McMahon raised a number of additional arguments on appeal. First, he argued that he lacked sufficient intent to manipulate because he was not aware of a scheme to manipulate the price and supply of ASWI. We do not credit this argument. Contrary to McMahon's contention, there is ample evidence that he knowingly participated in the manipulation of ASWI stock.[35] McMahon was Monitor's research analyst and admittedly had played a central role in bringing companies that Monitor wanted to market to the public to the attention of the sales force. He testified that in the regular course of his duties at Monitor, he reviewed prospective business deals that were presented to him by Pokross and he conferred with Palla regarding Monitor's market-making activity. In fact, although McMahon admitted at hearing that he knew that ASWI had no earnings prior to the commencement of trading on May 13-14, 1996, the evidence shows that he encouraged Monitor's sales force to make misrepresentations and baseless predictions to their customers in an effort to condition the market artificially for ASWI and facilitate the distribution of shares of ASWI to Monitor customers at

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[33] Mitchell Cushing ("Cushing") testified in his on-the-record interview that McMahon and Montelbano had been building up ASWI in an effort to get brokers to continue working at Monitor. Christopher Gonzales ("Gonzales") said that McMahon and Montelbano told the brokers that ASWI was "coming" and that it would be "a good thing for the firm."

[34] Cushing testified in his on-the-record interview that McMahon had showed him an article that indicated that Tivoli Systems had been bought by IBM and that McMahon also had advised him that the same individual who had been responsible for Tivoli was also responsible for ASWI. Similarly, Gonzales testified in his on-the-record interview that McMahon had given the brokers some articles about Tagliareni (ASWI's president and the person who had brought Tivoli public). Like Cushing and Gonzales, Herkert testified in his on-the-record interview that McMahon and Montelbano had talked to him about the fact that Tagliareni, ASWI's president, had started another company by the name of Tivoli that had gone public and had been sold to IBM for about $750 million. The record also contains documents that McMahon produced to staff in response to a request by NASD for documentation related to ASWI, pursuant to Procedural Rule 8210. This evidence includes news articles and marketing materials regarding Tivoli.

[35] Intent may be inferred from the facts and circumstances of a given case because manipulators usually do not publicize their intentions. See In re Fertman, 51 S.E.C. 943 (1994); In re Mawod & Co., supra at 870 n. 22 (citing Crane Company v. Westinghouse Air Brake Co., 419 F.2d 787, 794 (2d Cir. 1969), cert. denied, 400 U.S. 822 (1970)). Moreover, "[f]indings must be gleaned from patterns of behavior, from apparent irregularities, and from trading data. When all of these are considered together, they can emerge as ingredients in a manipulative scheme designed to tamper with free market forces." In re Pagel, supra. In addition, direct evidence of knowing participation in a manipulation strengthens the inferences to be drawn from such facts.

predetermined prices. McMahon also advised brokers that there were a limited number of shares, thus participating in the distribution as if it were an IPO; provided price projections; offered special compensation to certain brokers in the form of sales credits to induce them to sell ASWI shares to their customers; and told certain brokers the price at which ASWI would trade.[36] These actions demonstrate that McMahon participated in a manipulation of ASWI shares by intentionally interfering with the "free forces of supply and demand." See In re Pagel supra (citing United States v. Stein, 456 F.2d 844, 850 (2d Cir. 1972) ("The purpose of the [Exchange Act] is to prevent rigging of the market and to permit operation of the natural law of supply and demand").

Second, McMahon argued that he did not participate in every step of the manipulation.[37] There is, however, no requirement that an individual be involved in every stage of a manipulation to sustain a

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[36] As discussed earlier, there is no corroboration for McMahon's contention that he did not speak to brokers about ASWI or hold a "sales meeting" about ASWI prior to the commencement of trading on May 13-14, 1996. McMahon claims that he held a meeting about a company called Nevstar on or around May 16, 1996 (after the manipulative trading that occurred on May 13-14, 1996) and that brokers had asked him questions about ASWI on their own initiative at that time. We find that the great weight of evidence is contrary to this contention.

[37] Although the Hearing Panel found that the preponderance of the evidence demonstrated that McMahon knew that Monitor had been involved in the previous Rule 504 offering, we cannot by a preponderance of the evidence conclude that McMahon and Montelbano knew specifics about the Rule 504 offering. We also find no evidence to refute McMahon's and Montelbano's contention that they were unaware that control persons and/or owners of Monitor had participated in the Rule 504 offering and that they had obtained a cheap supply of ASWI stock at $1 per share.

McMahon and Montelbano argued that they were "surprised" when they found out on the morning of May 13, 1996 that ASWI had begun trading because they believed that ASWI was going to have an IPO in 1997. This argument is undermined by the evidence in the record. First, the record demonstrates that McMahon and Montelbano were aware that ASWI was not going to have an IPO. Montelbano testified that McMahon had advised him prior to the commencement of trading on May 13-14, 1996 that ASWI was not going to be an IPO, but was going to be a Rule 504 offering. Second, the evidence demonstrates that McMahon and Montelbano had been building up ASWI in an effort to retain Monitor brokers and had told them that ASWI was "coming" and that it would be "a good thing for the firm." Third, brokers testified that McMahon and Montelbano had made short-term price predictions in connection with ASWI that we have determined were unsubstantiated. Finally, McMahon's and Montelbano's claim that they were so upset when they found out that ASWI had commenced trading that they immediately left the Firm that day and met with a recruiter for a start-up company and the individual who was going to be the compliance director for the same company does not support their argument that they believed that ASWI was going to have an IPO in 1997. Whether they left the Firm that day to seek other employment is immaterial in light of the great weight of evidence

violation under Section 10(b) and Rule 10b-5. Section 10(b) and Rule 10b-5 prohibit the use of a manipulative device or scheme to defraud any person, "in connection with the purchase or sale of any security." The "in connection with" requirement has been construed broadly by the Supreme Court. See SEC v. Robert Hasho, 784 F. Supp. 1059 (S.D.N.Y. 1992) (citing Superintendent of Insurance v. Bankers Life and Casualty Co., 404 U.S. 6, 12 (1971)). McMahon's statements to Monitor brokers were meant to encourage them to persuade customers to purchase ASWI shares and, therefore, were made in connection with the purchase and sale of a security. Indeed, it was essential to the manipulative scheme that the Monitor sales force be mobilized to persuade customers to buy ASWI shares.

Third, McMahon argued that he had no motive to participate in a manipulation of ASWI shares because there is no evidence that he profited directly from the distribution. Evidence of a respondent's profit-making from a manipulation "is not talismanic." In re Brooklyn Capital & Secs. Trading, Inc., 52 S.E.C. 1286, 1293 (1997) (quoting In re R.B. Webster Investors, Inc., 51 S.E.C. 1269, 1274 (1994)); see also SEC v. U.S. Environmental, supra, at 112 (personal motivation for manipulating market is irrelevant in determining violation of Section 10(b)). Thus, it is irrelevant that McMahon appears not to have noticeably profited from the manipulation. Furthermore, the evidence indicates that he was entitled to override compensation on certain brokers' sales.

We find that McMahon participated in the manipulation by: (1) touting ASWI to Monitor brokers as a good investment for Monitor customers; (2) making misrepresentations about the prospects of ASWI, including the use of price predictions that had no reasonable basis;[38] (3) advising brokers that there were only a limited number of shares available for their customers as if the offering were an IPO; and (4) giving the brokers predetermined prices at which ASWI would trade, and promising predetermined sales credits in connection with the sales of ASWI shares.

Accordingly, we find that McMahon acted with the requisite intent by knowingly participating in the manipulation of the market for ASWI. We therefore affirm the Hearing Panel's findings that McMahon violated Section 10(b), Rule 10b-5, and Conduct Rules 2120 and 2110.

d. Montelbano Participated in a Manipulation of ASWI Shares. Brokers at the Broad Street office testified that Montelbano, who was Monitor's acting president during the relevant period,[39]

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that demonstrates that they were touting ASWI to brokers as a stock that Monitor would be selling in the near future.

[38] As noted earlier, ASWI's financial information showed that it had operated historically at a deficit. Further, the record does not include any information about ASWI's prospects that would support the representations and price predictions that McMahon made.

[39] Montelbano denies that he was Monitor's president, but the evidence demonstrates that he was

had: (1) advised a broker that there were a limited amount of ASWI shares that could be allocated to his customers and allocated ASWI shares to Monitor brokers as if the offering were an IPO;[40] (2) offered brokers special compensation in the form of credits;[41] (3) provided a price prediction;[42] and (4) told at least one broker the price at which ASWI would be offered.[43] Montelbano raised the same arguments as McMahon regarding the purported lack of credibility of the Monitor brokers who testified against him and his lack of intent to manipulate. We reject these contentions as having no merit, as discussed in our previous analysis. In sum, we find that Montelbano offered no credible evidence to refute the brokers' testimony concerning his involvement in the ASWI scheme. We find that Montelbano's actions were an attempt to induce Monitor brokers to sell ASWI shares at predetermined prices and with predetermined sales credits. We therefore find that the record contains sufficient evidence that Montelbano acted with the requisite manipulative intent by knowingly participating in a

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acting in that capacity during the relevant period. See note 75, infra, and text on pages 35-36 below.

[40] Herkert testified in his on-the-record interview that Montelbano had told him about ASWI a few days before trading in ASWI had commenced and that he had allocated a certain number of shares to him and his partner, Sierp. Herkert's testimony was corroborated by Sierp who testified at hearing that Montelbano and McMahon told him that they had 10,000 to 12,000 shares of ASWI stock that Sierp could place with his clients.

[41] See note 30, supra, for discussion.

[42] As discussed above, Telmany testified in his on-the-record interview that Montelbano and McMahon told him that ASWI was going to do very well and that it would be a $20 stock. We find this testimony to be reliable and probative because other brokers testified that McMahon had given them price projections (see note 24, supra, and text accompanying note) and that Montelbano and McMahon were together when they discussed ASWI with the Monitor sales force.

[43] As noted above, Telmany testified in his on-the-record interview that Montelbano and McMahon had advised him that ASWI would trade at a price of $8 or $8 1/4. We find this evidence to be reliable and probative in light of the testimony by other brokers who stated that McMahon had told them the price at which ASWI would trade and the testimony by a number of brokers that McMahon and Montelbano were together when they discussed ASWI with the Monitor sales force.

Although the Hearing Panel did not expressly conclude in the "legal analysis" section of its decision that Montelbano had provided information to brokers about the price at which ASWI would trade, the Hearing Panel made such a finding earlier in the decision in its discussion dealing with general findings against each respondent.

manipulation of ASWI shares.[44] Accordingly, we affirm the Hearing Panel's findings that Montelbano violated Section 10(b), Rule 10b-5, and Conduct Rules 2120 and 2110.

4. Sanctions for the Manipulation Violations

We find that bars in all capacities from participation in the securities industry are essential because respondents Galasso, McMahon, and Montelbano each knowingly took part in the manipulation of ASWI shares in violation of Rule 10b-5 and NASD Rules 2120 and 2110 and because of a number of aggravating factors, as detailed below.[45] Galasso engaged in activities to manipulate the price and supply of ASWI shares. In addition, he is singularly responsible for the trading of ASWI on May 13-14, 1996, and must accept responsibility for Monitor's manipulative trading practices. McMahon and Montelbano each participated in this manipulation by promoting ASWI to Monitor brokers and providing them with information about the price at which ASWI would trade and the sales credits associated with the sale of ASWI shares. McMahon and Montelbano also marketed the ASWI offering to the Monitor sales force like an IPO, which it was not, by advising brokers that they would be allocated a certain number of ASWI shares. McMahon and Montelbano also gave brokers misleading information about ASWI's prospects, including unsubstantiated price predictions. McMahon and Montelbano engaged in these activities in order to induce Monitor brokers to pitch ASWI shares aggressively to their customers.

We have considered the following aggravating factors in assessing sanctions: (1) the respondents' failure to accept responsibility for their actions; (2) McMahon's and Montelbano's insistence throughout these proceedings that they did not discuss ASWI with Monitor brokers prior to May 13, 1996; and (3) Galasso's, Montelbano's, and McMahon's attempts to blame others for the manipulation involving ASWI shares. We agree with the Hearing Panel that even if Galasso, Montelbano, and McMahon were "used" by others to further the fraudulent scheme, there is no evidence that they were anything other than willing participants in its execution.

In light of the foregoing, we conclude that Montelbano, McMahon, and Galasso pose a threat to the public interest if allowed to continue in the securities industry. We therefore affirm the Hearing Panel's imposition of a bar from associating with any member firm in any capacity as to Galasso,

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[44] We do not affirm the Hearing Panel's finding that Montelbano also provided brokers with certain baseless information about ASWI. The record contains insufficient evidence for us to conclude that he engaged in such activities.

[45] There are no applicable Sanction Guidelines directly addressing violations of Section 10(b) and Rule 10b-5 for manipulation. The Commission has made clear, however, that manipulation is a serious offense that warrants significant sanctions. See In re Pagel, supra, at 232 (manipulation "attacks the very foundation and integrity of the free market system" and in crafting sanctions for such conduct there is "no basis for leniency").

McMahon, and Montelbano. We also affirm the Hearing Panel's imposition of monetary fines in the following amounts: $50,000 as to McMahon; and $40,000 as to Montelbano. We increase Galasso's monetary fine to the same level as McMahon's ($50,000) because of the nature of his involvement in the manipulation of the prices of ASWI. Finally, like the Hearing Panel, we order that such fines be suspended until such time as McMahon, Montelbano, and Galasso may seek to re-enter the securities industry.[46]

B. Rule 10b-6 Allegation Against Galasso, McMahon, and Montelbano

Rule 10b-6 was an anti-manipulation rule intended to prevent persons participating in a distribution of securities, as defined in the rule, from artificially conditioning the market for the securities in order to facilitate the distribution, and to protect the integrity of the securities trading market as an independent pricing mechanism.[47] See Review of Antimanipulation Regulation of Securities Offerings, Exchange Act Rel. No. 33924 (April 19, 1994). Rule 10b-6 prohibited persons or entities engaged in a "distribution" of securities from bidding for or purchasing for their own account the security being distributed until after the completion of the distribution or from attempting to induce other persons to purchase the security being distributed.[48]

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[46] Our decision to impose a fine is consistent with NASD Notice to Members "NTM" 99-86 (Oct. 1999) (Imposition and Collection of Monetary Sanctions), which provides, among other things, that NASD Regulation generally will pursue the collection of any fine in sales practice cases, even if an individual is barred, if there has been widespread, significant, and identifiable customer harm. The Hearing Panel, however, decided to suspend the fines it imposed until respondents seek to re-enter the industry. The suspension of fines was not argued on appeal, thus, for procedural reasons, we have determined to suspend any fines imposed on the respondents in this matter until such time as they may seek to re-enter the securities industry. While we have decided to suspend the fines imposed in this particular matter, we normally would not suspend fines in these circumstances pursuant to the policy articulated in NTM 99-86.

We have decided to affirm a slightly higher fine for McMahon than the fine for Montelbano in light of his direct involvement with ASWI, his knowledge of its business plan, and the specific unsupported information he gave to the brokers concerning the future potential of the company. We have decided to increase the fine that the Hearing Panel imposed for Galasso from $40,000 to $50,000 in light of his direct involvement in the manipulative trading activity.

[47] The Commission adopted a comprehensive revision of Rule 10b-6 that became effective on March 4, 1997. These revisions made Rules 101 and 102 under Regulation M successor rules to Rule 10b-6. See Anti-Manipulation Rules Concerning Securities Offerings, Exchange Act Rel. No. 38067 (Dec. 20, 1996). Since the conduct at issue here occurred prior to the effectiveness of the revisions, Rule 10b-6 is applicable in the present case.

[48] Rule 10b-6 applied to issuers, selling shareholders, underwriters, prospective underwriters,

The prohibitions contained in Rule 10b-6 applied to "distributions." Rule 10b-6 defined a distribution as an offering of securities distinguished from ordinary trading transactions by the "magnitude" of the offering and the presence of "special selling efforts and selling methods." See Rule 10b-6(c)(5). Factors relevant to the magnitude element include the number of shares for sale, the trading volume that those shares represent, the percentage of outstanding shares, and the public float. See Exchange Act Rel. No. 33924, supra; In re First Albany Corp., 50 S.E.C. 890 (1992); In re J.H. Goddard & Co., Exchange Act Rel. No. 7618 (June 4, 1965); In re Bruns, Nordeman & Co., Exchange Act Rel. No. 6540 (Apr. 26, 1961). In December 1995, Monitor control persons and their affiliates purchased 485,000 out of the 535,000 publicly tradeable shares in ASWI that were offered through the Rule 504 private placement. Monitor control persons transferred 125,000 of those shares to Baird Patrick for the account of DMN. On May 13-14, 1996, Monitor purchased 124,500 ASWI shares (23% of the publicly tradable float) and sold 120,600 ASWI shares to its retail customers. Moreover, Monitor was the only market maker and was involved as buyer or seller in 100% of the ASWI trades on those dates. We thus adopt the Hearing Panel's determination that the sales effort satisfied the "magnitude" element of Rule 10b-6.[49] See Collins Securities Corp. v. SEC, 562 F.2d 820 (D.C. Cir. 1977); In re Billings Associates, Inc., 43 S.E.C. 641, 648 (1967); In re J.H. Goddard & Co., Inc., 42 S.E.C. 638 (1965); In re Bruns, Nordeman & Co., supra.

We also agree with the Hearing Panel's determination that the transaction satisfied the "special selling efforts" element of a "distribution." The Commission has stated that the presence of special selling efforts may be indicated in a number of ways, including the payment of compensation greater than that normally paid in connection with ordinary trading transactions. The Commission has also found evidence of special selling efforts when a firm's sales force has been mobilized to sell a particular stock. For example, in In re First Albany, supra, the Commission found evidence of special selling efforts when, as part of the daily announcements to the branch offices, representatives from First Albany's research and trading departments described the stock; referred to the research report that had been distributed to the firm's registered representatives by that date; informed the firm's registered representatives that the firm had a substantial position in the stock; and advised the registered representatives of the desirability of selling the stock.

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dealers, brokers, and other persons who had agreed to participate or were participating in the distribution, as defined in Rule 10b-6(c)(5), and their "affiliated purchasers," as defined in Rule 10b-6(c)(6), including broker-dealer affiliates.

[49] See Exchange Act Rel. No. 33924, supra. The Hearing Panel also observed that it was not challenged by any respondent that the distribution of ASWI on May 13-14, 1996 met the magnitude requirement of Rule 10b-6.

In the present case, the evidence demonstrates that McMahon and Montelbano were involved in mobilizing the Monitor sales force to sell ASWI. McMahon and Montelbano touted ASWI to Monitor brokers for at least a week prior to the commencement of trading in an effort to have Monitor brokers persuade their customers to purchase shares of ASWI. As part of their effort to induce brokers to sell ASWI shares to their customers, McMahon and Montelbano offered a special "sales credit" to brokers and allocated ASWI shares to certain brokers and in fact the original ASWI order tickets reflected a $2.25 credit per share, or 33% of the price of the shares sold, as a commission to Monitor brokers. We find that this extraordinary compensation was a significant inducement to the sales force. Galasso admitted that the sales credits and prices at which the ASWI trades would be executed had been predetermined and that the brokers knew the amount of sales credit that they would be receiving prior to the commencement of trading.[50] Moreover, the evidence shows that Galasso executed the trades with predetermined sales credits and at predetermined prices. The combination of these factors provide compelling evidence that Monitor engaged in special selling efforts with respect to ASWI.

Because the ASWI transaction satisfied the two characteristics of a distribution (the magnitude of the offering and the presence of special selling efforts), we conclude that the transaction, through the participation of McMahon, Montelbano, and Galasso, constituted a "distribution" of ASWI shares. We now examine whether the individual respondents violated the prohibition in Rule 10b-6 against manipulative trading practices.

1. Galasso Violated Rule 10b-6. We find that Galasso displayed ascending bids for ASWI on May 13, 1996 for the purpose of creating actual, or apparent, active trading in or raising the price of ASWI while participating in a distribution of ASWI shares. After raising its bid 10 times in approximately two hours (from $.875 to $6.75) through Galasso's actions, Monitor distributed 120,500 ASWI shares to Monitor's retail customers on May 13-14, 1996.[51] This sharp increase in price was not supported by any meaningful demand and permitted Monitor to sell the ASWI shares to retail customers at inflated levels. Rule 10b-6 was designed to prevent the exact type of manipulation in which Galasso engaged -- bidding for ASWI shares for manipulative purposes while also distributing the

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[50] Galasso's testimony regarding the fact that sales credits had been predetermined is corroborated by Monitor brokers who testified that they had been given information about the amount of sales credits associated with the sales of ASWI shares prior to the commencement of trading on May 13-14, 1996. See discussion above on pp. 13-15. Additionally, Leverett testified at hearing that the mark-up that he was going to receive on the ASWI transactions that he effected for two of his customers was predetermined.

[51] The majority of the sales to retail customers were effected at $6.75 on May 13, 1996 and at $6.375 on May 14, 1996.

shares to the public. Accordingly, we affirm the Hearing Panel's finding under cause sixteen that Galasso knowingly violated Rule 10b-6 and Conduct Rules 2110 and 2120.[52]

2. There Is Insufficient Evidence To Find That McMahon and Montelbano Violated Rule 10b-6. The Hearing Panel found that McMahon and Montelbano had engaged in a distribution of ASWI shares by, among other things, informing brokers that they would receive special compensation for selling ASWI shares and by allocating ASWI shares to certain brokers in violation of Rule 10b-6. While those activities are evidence of "special selling efforts," one of the elements necessary to find that a particular transaction constituted a "distribution" for purposes of Rule 10b-6, and while we have found ample evidence to support their individual participation in the ASWI manipulation, we find that there is insufficient evidence that McMahon and Montelbano, while participating in a distribution, bid for or purchased for any account that they had a beneficial interest, a security which is the subject of such distribution, or attempted to induce any person to purchase such security which is the subject of a distribution. Accordingly, we reverse the Hearing Panel's finding of violation and dismiss the Rule 10b-6 allegations in cause sixteen against McMahon and Montelbano.

3. Sanctions for Rule 10b-6 Violation.

We find that the level of sanctions we are imposing on Galasso for the manipulation violations are equally appropriate for the Rule 10b-6 violation.[53] Thus, we reverse the Hearing Panel's determination not to impose separate sanctions for the Rule 10b-6 violation.

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[52] We find that there is sufficient evidence to conclude that Galasso acted with scienter with respect to the violation of Rule 10b-6. The SEC has stated that:

> A person contemplating or making a distribution has an obvious incentive to artificially influence the market price of the securities in order to facilitate the distribution or to increase its profitability. [The Commission has] accordingly held that where a person who has a substantial interest in the success of a distribution takes active steps to increase the price of the security, a prima facie case of manipulative purpose exists.

Exchange Act Rel. No. 33924, supra, at 5.

[53] We hold that either violation, standing alone, would justify a bar and $50,000 fine, but find that it is unnecessary to impose cumulative sanctions for the two violations.

C. Monitor's Excessive Mark-Ups on ASWI Transactions

We agree with the Hearing Panel's determination that Monitor dominated and controlled the market for ASWI and that any mark-ups therefore should have been based on the "contemporaneous cost" at which Monitor acquired ASWI shares.[54] We therefore concur with the Hearing Panel's decision that the best evidence of Monitor's contemporaneous costs with respect to the ASWI transactions on May 13-14, 1996 are the prices that Monitor paid to Baird Patrick for ASWI shares which were the closest in time to the sales that Monitor effected with its retail customers on those dates.[55] Hence, Monitor's contemporaneous cost for ASWI on May 13, 1996 was $3.875 per share, and on May 14, 1996, was $5 per share. Based on those contemporaneous costs, Monitor, acting through Galasso, charged excessive mark-ups to Monitor customers, the majority of which were well above the acceptable limits contemplated by the NASD's Mark-Up Policy.[56] These transactions (107

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[54] See domination and control discussion above on p. 10. A mark-up is the difference between the retail price and the "prevailing market price" of a security. In re Alstead, Dempsey & Co., Inc. 47 S.E.C. 1034, 1035 (1984). Except in domination and control situations, when a market maker is involved, mark-ups may be computed using the price charged by the firm or other market makers in actual sales to other dealers. Id.; Orkin v. SEC, 31 F.3d 1056 (11th Cir. 1994). It is well established, however, that when a firm dominates the market to such a degree that it controls wholesale prices for the security, the price that the dominating and controlling dealer is willing to pay other dealers, known as the firm's "contemporaneous cost," is the best evidence of prevailing market price. See In re Frank L. Palumbo, 52 S.E.C. 467 (1995); In re George Salloum, 52 S.E.C. 208 (1995); Meyer Blinder, supra, at 1218.

[55] Enforcement provided two schedules for calculating mark-ups in the proceedings below. The first schedule calculated mark-ups based on $1, the price paid for ASWI shares in the Rule 504 offering by Monitor control persons and their associates. The second schedule calculated mark-ups based on Monitor's contemporaneous cost in acquiring ASWI shares on May 13-14, 1996. Enforcement argued in the proceedings below that because Monitor's owners controlled the DMN account from which Monitor purchased all of the ASWI shares it resold to its customers, $1 would be the proper basis upon which to review mark-up charges. The Hearing Panel determined that the price paid for ASWI shares in the Rule 504 offering was the firm's "historical" cost and thus not a measure of the prevailing market price of the firm's contemporaneous costs of acquiring the shares from Baird Patrick on May 13-14, 1996 ($3.875 on May 13 and $5 per share on May 14). We agree with the Hearing Panel's determination. The NASD's Mark-Up Policy states that a retail price is unfair if it is "not reasonably related to the current market price of the security." (emphasis added) IM-2440 ("Mark-Up Policy").

[56] Under the NASD's policy, mark-ups for equity securities greater than 5% above the prevailing market price generally are considered unreasonable and, thus, violative of NASD rules. See Conduct Rule 2440 and IM 2440; see also NASD Notice to Members 92-16, at 91 (April 1, 1992). The Hearing Panel found, and we concur, that the mark-ups, which ranged from 6.45% to 74.19% were excessive in light of the totality of the circumstances. In fact, the vast majority of the excessive mark-

in total) resulted in excessive mark-ups (mark-ups exceeding 5%) of $221,931. All but one of these transactions (a total of 106 transactions), exceeded 10% and, thus, were fraudulent per se.[57] Accordingly, we find that those mark-ups were excessive, and except for one transaction, fraudulent.

1. Galasso Was Responsible for the Firm's Excessive and Fraudulent Mark-Ups. We find that, as the Firm's trader, Galasso executed the ASWI transactions with sales credits to Monitor brokers which resulted in excessive and fraudulent mark-ups. Significantly, Galasso conceded that he had executed the ASWI trades, at the direction of Palla, at predetermined prices with predetermined credits and admitted that he might have said that he thought the mark-ups were excessive.[58] The Commission has stated that a firm trader is charged with "knowing fundamental standards for charging fair prices to the public," including those governing a dominated and controlled market, and that his reckless disregard for these standards satisfies the scienter requirement. See e.g., In re G.K. Scott & Co., Inc. 51 S.E.C. 961, 968 (1994), aff'd (table case) 56 F.3d 1531 (D.C. Cir. 1995).

We accordingly affirm the Hearing Panel's finding that under cause fifteen Galasso violated Conduct Rules 2110, 2120, and 2440, Section 10(b), and Rule 10b-5. We find that Galasso knew that the Firm dominated and controlled the market for the ASWI shares and that customers would be charged excessive and fraudulent (as to those greater than 10%) mark-ups if those mark-ups were not based on the Firm's contemporaneous cost. Thus, we find that the requisite degree of scienter has been shown to support the Hearing Panel's finding that Galasso violated Section 10(b) and Rule 10b-5.

(continued)
ups ranged from 27.50% to 74.19%, far exceeding the acceptable limits set forth under the NASD's Mark-Up Policy.

[57] See, e.g., SEC v. First Jersey Securities, Inc. 101 F.3d 1450, 1469 (2d Circuit 1996) (an undisclosed mark-up of more than 10% above the prevailing market price has been held to constitute fraud per se); Orkin v. SEC, supra, at 1063 ("The SEC has consistently held that a markup of more than 10% in the sale of equity securities is unfair or fraudulent"). The Hearing Panel decided not to place the five transactions with mark-ups of 10.48% in the fraudulent per se category. We disagree with that determination and find that these five transactions that exceeded 10% are fraudulent per se.

[58] The Hearing Panel found that: (1) on May 13, 1996, Galasso executed order tickets at a price of $6.75, which included a sales credit of $2.25 for the brokers at the Third Avenue office, and at a price of $6.50, which included a sales credit of $1.25 for the brokers at the Broad Street office; and (2) on May 14, 1996, Galasso executed the 30 order tickets from Broad Street that had been marked "not done" the day before at a price of $6.375 with sales credits of $1.25. The Hearing Panel determined that Galasso knew the prices were predetermined, knew the prices included special compensation to the brokers, and knew the mark-ups were excessive. We affirm these findings.

2. Sanctions for Excessive and Fraudulent Mark-Up Violations. The Sanction Guideline for Rule 2440 violations recommends a 30-day suspension and, in egregious cases, imposition of a suspension for up to two years or a bar.[59] It also suggests the imposition of fines ranging from $5,000 to $100,000, plus the gross amount of the excessive mark-ups.[60]

We have concluded that this is an egregious case in light of the number of excessive mark-ups that were fraudulent (106 out of 107) that Galasso executed and the amount of the gross profits above 5% ($221,931) involved.[61] In assessing sanctions, we considered the egregious nature of Galasso's misconduct and the following aggravating factors: (1) that Monitor dominated and controlled the market in ASWI, which is one of the principal considerations listed in the Guideline; and (2) that Galasso failed to take any responsibility or express any remorse for his actions throughout these proceedings. In light of all of these factors, we find that Galasso should be barred from association with any member firm in any capacity. Furthermore, we conclude that a bar is essential to protect investors.

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[59] See NASD Sanction Guidelines (1998 ed.) at 82 (Excessive Mark-ups).

[60] We are troubled by the Hearing Panel's decision not to increase its fine or to impose a restitution requirement based on the amount of excessive mark-ups with respect to this cause. See Sanction Guideline for Excessive Mark-Ups (1998 ed.) at 82; NASD Regulation NTM 99-86. The Guideline recommends that the monetary sanction include the gross amount of the excessive mark-ups, if restitution is not ordered. In addition, the policy set forth in NTM 99-86 provides that NASD Regulation generally will require the payment of restitution and disgorgement in sales practice cases where there has been widespread, significant, and identifiable customer harm. With respect to its decision not to impose disgorgement of the gross amount of the excessive mark-ups, the Hearing Panel stated that such disgorgement was not appropriate because there was no evidence that Galasso received directly any portion of the excessive profits. Although we do not endorse the rationale for this determination, we find the sanctions that we sustain in this regard to be sufficient in the overall context.

[61] Galasso, as the Firm's sole trader during the relevant period, executed each ASWI transaction resulting in an excessive mark-up. Galasso argued that he was only executing the tickets at the price he was given by the brokers and that he did not determine the amount of the mark-ups. Nevertheless, as the only trader at Monitor on May 13-14, 1996, Galasso had a responsibility to the Firm's customers to ensure that the prices they paid for ASWI shares were reasonably related to the market. The fact that Leverett admitted that he was responsible for reviewing mark-ups and commissions when Palla was out of the office does not relieve Galasso from his responsibility as a trader. Galasso admitted that he made no effort to get a better price for Monitor's customers than was written on the order tickets because he was "instructed to print the tickets exactly the way they were written to me." "A trader has the responsibility to charge fair mark-ups and is not relieved of that obligation because the firm or its compliance officers approved or even directed his method of calculating mark-ups." See Jeffrey Field, supra.

Accordingly, we affirm the Hearing Panel's imposition of a bar from associating with any member firm in any capacity and a fine of $30,000, which is suspended until such time as Galasso may seek to re-enter the securities industry.[62]

D. Manipulative and Deceptive Sales Practice Allegations Against Leverett and Nejaime

1. The Evidence Does Not Support The Allegations in the Complaint as to Leverett. We called this matter for review to analyze the appropriateness of the findings and sanctions that the Hearing Panel imposed as to Leverett in the proceedings below. The complaint alleged that Leverett knowingly or recklessly engaged in manipulative and/or deceptive trading practices conditioning the market artificially to facilitate the distribution of shares of ASWI to his clients, in violation of Section 10(b), Rule 10b-5, and Conduct Rules 2110 and 2120. The complaint further alleged that Leverett accomplished this objective by making certain specific misrepresentations to two clients in an effort to solicit the purchase of ASWI shares by those customers. The complaint alleged: (1) that Leverett told customer J.C. that ASWI was an IPO; and (2) that Leverett told customer F.M. that he (Leverett) had researched the company and that it would "go up a point or two," when, in fact, he had conducted no such research.

The Hearing Panel found insufficient evidence to conclude that Leverett had told customer J.C. that ASWI was an IPO.[63] Based on our independent review of the evidence, we concur with the Hearing Panel's determination. As to the second customer, the Hearing Panel decided not to accept the statements in F.M.'s declaration as evidence against Leverett since the declaration had not been executed under oath and the customer did not participate in the hearing. We note that the unsworn declarations of customers who have not testified, although hearsay, are admissible and can be reliable and probative if corroborated by other evidence. In re Kevin Lee Otto, Exchange Act Rel. No. 43296 (September 15, 2000) (customer's complaint letters and annotations that were corroborated by other evidence found to be reliable and probative); In re Mansfield, 46 S.E.C. 356 (1976) (customer complaint letters that were corroborated by other evidence found to be reliable and probative). In this instance, however, there is no circumstantial or direct evidence in the record to corroborate F.M.'s statement. Thus, we find insufficient evidence to conclude that Leverett misled F.M. as to ASWI's prospects.

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62 See note 46 above.

63 J.C. testified at hearing that he had no recollection as to the basis for his belief that ASWI was an IPO and his declaration did not state that Leverett told him it was an IPO. J.C. testified that the basis for his belief was either that Leverett had told him or that he (J.C.) assumed it was an IPO based on the prior deal he had done with Leverett.

The Hearing Panel made additional findings that Leverett engaged in deceptive sales practices by recommending ASWI to J.C. without a reasonable basis and by selling shares to his customers J.C. and F.M. at predetermined prices without regard to market demand. The complaint, however, failed to allege these violations. The complaint alleged only that Leverett had engaged in manipulative and deceptive sales practices by making specific misrepresentations, as detailed above, to two of his customers. We have found that there is insufficient evidence that Leverett made any of the misrepresentations alleged in the complaint, and thus must dismiss this cause of action. Accordingly, we dismiss the allegations in cause 13 that Leverett engaged in manipulative and/or deceptive trading practices in violation of Section 10(b), Rule 10b-5, and Conduct Rules 2110 and 2120.

2. The Evidence Does Not Support The Allegations in the Complaint as to Nejaime. We called this matter for review to examine the findings and sanctions that were imposed by the Hearing Panel as to Nejaime in the proceedings below. The complaint alleged that Nejaime was the de facto sales manager of Monitor's Third Avenue office and that he knowingly or recklessly had engaged in manipulative or deceptive trading practices in violation of Section 10(b), Rule 10b-5, and Conduct Rules 2110 and 2120. The complaint also alleged that Nejaime engaged in activities to condition the market artificially to facilitate the distribution of shares of ASWI to Monitor customers at predetermined prices by creating or permitting to be created a "boiler room" which facilitated the use of price predictions without any reasonable basis, misrepresentations, and the use of other high-pressure sales tactics in the marketing of ASWI to Monitor customers. Additionally, the complaint alleged that Nejaime acted to further the scheme of manipulation and deception of Monitor customers by coordinating the solicitation of indications of interest and by advising Monitor brokers of their allocations of ASWI.

The Hearing Panel first found that, notwithstanding Nejaime's purported title of "managing director," and the fact that he had some administrative responsibilities at Third Avenue beyond that of a broker, Nejaime was not a "manager" or supervisor. We find that the record supports this conclusion. Although there is evidence in the record that Nejaime asked one of the brokers (Hogan) in the Broad Street office to write down his indications of interest for ASWI shares so that he could be allocated a certain number of ASWI shares, the Hearing Panel concluded that such evidence, standing alone, was insufficient to support a finding that Nejaime "coordinated" the allocation process. The record contains no evidence that Nejaime either asked any other brokers to provide indications for ASWI shares or allocated any ASWI shares to Monitor brokers. Therefore, we affirm the Hearing Panel's finding that there was insufficient evidence to find a violation with respect to this allegation.

The Hearing Panel determined, however, that Nejaime had participated in the ASWI scheme by selling shares to his customers at predetermined prices having nothing to do with the prevailing market price, and that he knowingly concealed his compensation from his customers. We find that the complaint does not allege such misconduct and that making a finding under this alternative theory would be inappropriate.

Accordingly, since the allegations in the complaint are unsupported by the evidence in the record, we dismiss the allegations of cause 14 that Nejaime engaged in manipulative and deceptive trading practices in violation of Section 10(b), Rule 10b-5, and Conduct Rules 2110 and 2120.

E. False and Fictitious Records

Monitor did not produce to NASD staff the original order tickets for the ASWI trades that had been executed on May 13-14, 1996. Clifton Miskell, a supervisor at Monitor's clearing firm, RAF Financial Corporation ("RAF"), testified that he had received from Monitor a set of order tickets on May 13-14, 1996 that were the original order tickets, and that Monitor later canceled and rebilled the original order tickets twice. First, on May 14, 1996, Monitor canceled and rebilled 65 customer orders that had been executed on May 13, 1996 because the CUSIP number was incorrect. Second, on May 16, 1996, Monitor canceled and rebilled the trades that had occurred on May 13-14, 1996, this time to reduce the sales credit on the tickets by as much as $1.00 to $1.25 per share.[64] NASD examiner Shields testified that the change in the price of the commissions did not impact the customers because they paid the same price for the shares that they had been charged in the original transactions.[65] The net effect of changing the commissions was that the amount received by the brokers was reduced and the amount Monitor received was increased.

Procedural Rule 8210(a)(1) authorizes NASD Regulation to require persons associated with a member of the NASD to "provide information . . . if requested, with respect to any matter involved in any investigation," and Rule 8210(c) imposes on associated persons and member firms an unqualified obligation to fully and promptly cooperate with requests made by NASD Regulation under Rule 8210. In addition, Conduct Rule 3110 requires member firms "to keep and preserve books, accounts, records, memoranda, and correspondence in conformity with all applicable laws, rules, regulations, and statements of policy promulgated thereunder and with the Rules of the Association." Falsifying records is a violation of Conduct Rule 3110 and is also inconsistent with the requirement in Conduct Rule 2110 that members, in the conduct of their business, observe high standards of commercial honor and just and equitable principles of trade.[66] See In re Douglas John Mangan, Complaint No. C10960612 (NAC,

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[64] Although the Hearing Panel found that the May 13 order tickets had been canceled and rebilled to lower sales credits, it overlooked the testimonial and documentary evidence in the record that demonstrates that the May 14 order tickets also had been canceled and rebilled to lower sales credits.

[65] The reported price also had been lowered on the canceled and rebilled tickets but that did not affect the price that the customers paid because the execution price had not changed and the execution price was the price at which the trades were processed by Monitor's clearing firm.

[66] NASD General Provision 115(a) states that persons associated with a member have the same duties and obligations as a member under the NASD's rules. Thus, Conduct Rule 3110 applies to individuals associated with a member as well as to associated persons.

July 29, 1998) (the NAC sustained a Conduct Rule 3110 violation for creating false customer records); In re George L. Pelaez, et al., Complaint No. C07960003 (NAC, May 22, 1997).

1. Galasso Falsified Trade Tickets To Reflect No Compensation to Monitor Brokers. Cause 18 of the complaint alleged that Galasso took affirmative steps to ensure that trade confirmations for ASWI would not reflect any compensation to the Firm or broker by ensuring that the "reported price," "execution price," and "limit price" indicated on the tickets that he processed were the same, even though this information did not accurately reflect the transactions which occurred. The complaint further alleged that, as a result, the Firm sent its customers trade confirmations that reflected no compensation to brokers on ASWI trades.

The Hearing Panel found that the customer trade confirmations for ASWI did not reflect any compensation to the Firm or brokers because Galasso had ensured that the reported price, execution price, and limit price indicated on the tickets were the same, even though the information on the tickets did not accurately reflect the transactions. We find that the evidence in the record supports this conclusion.

The majority of the order tickets that Galasso executed for the ASWI trades had the same price indicated for the "reported price," "execution price," and "limit price." Indeed, Galasso admitted that when he started making markets at Monitor he had been instructed to process Monitor order tickets with the reported price, executed price, and limit price all the same and to ensure that no mark-ups were indicated to Monitor customers.[67] In addition, the customer confirmations that were included in

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[67] Galasso testified as follows at his February 5, 1997 on-the-record interview:

> Galasso: They didn't want to show it as mark-ups. They wanted a reported price, an executed price and a limit price all the same, okay? And as no commission.
>
> Q. As no mark-up?
>
> Galasso: As no mark-up.
>
> Q. The confirm would show reported price and net the same?
>
> Galasso: Reported price, net the same, price the same, no mark-up. So it looks like the customer was just buying the stock for free. . . .
>
> Q. Who told you to do that?
>
> Galasso: This is what I learned to do when I started making markets at Monitor.

the record do not reflect any mark-ups or commissions. Galasso, the Monitor brokers who testified, and Leverett all denied having filled in the reported and execution prices and the sales credit amounts on the ASWI order tickets. Nonetheless, based on Galasso's admission about the manner in which he had been instructed to process Monitor order tickets and our collective industry expertise and experience in these matters, we conclude that Galasso ensured that the limit, execution, and reported prices were all the same so that no mark-up or commission would be revealed to Monitor customers on the trade confirmations.[68]

Accordingly, we affirm the Hearing Panel's finding that Galasso assisted in the creation of false trade confirmations by ensuring that the limit price, reported price, and execution price were the same on all the order tickets in violation Conduct Rule 3110 and 2110, as alleged in cause 18 of the complaint. We reverse, however, the Hearing Panel's finding that Galasso remitted an incomplete set of order tickets in response to a NASD Rule 8210 request because the complaint did not allege that the NASD had directed a request for the original order tickets to Galasso. Thus, we dismiss the Hearing Panel's finding of violation as to Rule 8210.

2. Leverett Reviewed and Approved Altered Order Tickets. We called this matter for review in part to analyze the Hearing Panel's dismissal of cause 17, which contained two allegations involving Leverett. First, it alleged that Monitor, through Leverett and others, had produced ASWI order tickets that it represented were the original order tickets for trades executed by its Third Avenue office on May 13, 1996 that were time-stamped between 3:26 and 3:36 p.m. and that reflected a commission of $0.25 or less, and that Monitor failed to produce the "original" order tickets that had been executed between 4:24 p.m. and 4:36 p.m. at a price of $6.75 per share, with a credit to the brokers of $2.25. Instead of making a finding on these allegations as to Leverett, the Hearing Panel concluded that the evidence did not support a finding that Leverett had failed to provide to the NASD the original tickets for his two customers -- an allegation different from the allegations in the complaint.[69] Although we

(continued)

Q. From?

Galasso: Bill [Palla] introduced me to it. And that's how it went.

[68] We infer from Galasso's testimony as set forth in note 67, supra, that he ensured that the order tickets had the same amount filled in for the limit, execution, and reported price, notwithstanding his testimony that he did not "write" the ASWI order tickets. See note 22, supra, and text accompanying note, regarding Galasso's claim that he did not "write" the order tickets at issue.

[69] The Hearing Panel apparently adopted the position that Enforcement advocated in its Post-Hearing Brief (submitted after the hearing in the proceedings below), in which it argued that Leverett had "violated Rule 8210 by failing to provide the NASD staff with order tickets for his own two customers."

affirm the Hearing Panel's determination that the evidence does not support a finding that Leverett violated Rule 8210, we do so on a different basis than the one set forth in the Hearing Panel's decision.

There is no evidence in the record that NASD Regulation asked Leverett to provide the original order tickets for the ASWI trades or that he was the individual who submitted the ASWI order tickets that had been canceled and rebilled. Accordingly, we dismiss the allegation that Leverett failed to produce the original tickets for the ASWI trades that were executed on May 13-14, 1996, in violation of Rule 8210.

Cause 17 also alleged, however, that the order tickets that the Firm produced to NASD Regulation were falsified and that Leverett had reviewed and approved them in violation of Rules 2110 and 3110. We find sufficient evidence in the record to support this allegation and disagree with the Hearing Panel's decision to dismiss this allegation. Leverett was the only principal working in the Third Avenue office during the relevant period, and he initialed some of the original order tickets and all of the canceled and rebilled tickets, which included the lower sales credit amount. The Hearing Panel concluded that it could not presume that Leverett knew that the canceled and rebilled tickets were false just because they were different from the original order tickets. We note, however, that the Hearing Panel's finding in this regard is inconsistent with the credibility determinations it made as to Leverett in its discussion of the supervision allegations against him. The Hearing Panel specifically discredited Leverett's testimony that he did not recall the ASWI tickets' having been canceled and rebilled, and noted that there was evidence that demonstrated that he was involved in canceling and rebilling over 50 ASWI order tickets (he in fact initialed all of the ASWI order tickets that had been canceled and rebilled).[70] We adopt this finding. Additionally, Leverett's claim not to have recalled cancels and rebills is further undermined by his admission at hearing that he had written two sets of order tickets with respect to his own customers -- J.C. and F.M.

We reverse the Hearing Panel's dismissal of the allegation that Leverett reviewed and approved falsified order tickets in violation of Rules 2110 and 3110. The record demonstrates: (1) that Leverett was one of the principals at the Firm that NASD Regulation staff spoke to on May 16, 1996 as part of NASD's investigation of ASWI trading on May 13-14, 1996 and that he was therefore on notice that

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[70] Leverett testified that his initials signified that he had reviewed the tickets. The Hearing Panel rejected Leverett's testimony that his initials on the tickets signified not that he had "approved" the ticket, but rather, that he had just "looked" at the tickets. We agree with the Hearing Panel's credibility determination. We also agree with the Hearing Panel's determination to discredit Leverett's statement that he did not specifically recall reviewing any of the ASWI tickets but was sure that when he did sign the order tickets there was only a limit price on each ticket and the tickets did not include a sales credit. The Hearing Panel concluded that Leverett's contention made no sense because he would not have been able to determine excessive mark-ups or commissions, which admittedly was his purpose for reviewing the order tickets, if only limit prices were on the tickets.

there was a potential problem with the trades that had occurred on those dates; (2) that Leverett admitted he had written two sets of ASWI order tickets for two of his customers; (3) that Leverett's initials appeared on some of the original order tickets and on all of the canceled and rebilled tickets; and (4) that Leverett admitted that his purpose for reviewing and initialing order tickets was to check for excess mark-ups or commissions. In addition, as discussed above, Leverett's denial of knowledge of the cancels and rebills is not credible. Based upon these facts and findings, we find that Leverett was aware that the cancels and rebills were prepared to lower the amount of the sales credit and that he thus reviewed and approved the falsified tickets, as alleged in the complaint. Accordingly, we reverse the Hearing Panel's dismissal of the allegation and find under cause 17 that Leverett violated Conduct Rules 3110 and 2110.

3. Sanctions for False and Fictitious Records Violations. The Hearing Panel imposed combined sanctions of a bar and a $30,000 fine (to be suspended until such time as he attempts to re-enter the securities industry) on Galasso for failing to turn over the original order tickets in response to a request from NASD Regulation staff in violation of Rule 8210 and for his ensuring that each order ticket had the same execution, reported, and limit price, resulting in the generation of false and misleading trade confirmations, in violation of Rules 2110 and 3110. Because we reverse the Hearing Panel's finding that Galasso violated Rule 8210 by failing to turn over the original order tickets in response to a request by NASD and are left with only the recordkeeping violation, we reduce the sanctions.[71] The Guideline for Rule 3110 violations recommends suspending the responsible party for up to 30 business days and a fine of $1,000 to $10,000.[72] In egregious cases, the Guideline recommends a lengthier suspension (of up to two years) or a bar. In reaching a sanction, we have considered that Galasso's actions were deliberate and that, at the time of the misconduct, he had been in the securities business long enough to know that the falsification of order tickets was violative of NASD rules. Thus, we consider Galasso's conduct to be egregious and, therefore, look to the upper end of the range of sanctions recommended for such conduct under the Guideline for recordkeeping. Accordingly, Galasso is suspended for one year from associating with any member firm in any capacity and fined $10,000 (such fine to be suspended until such time as he may seek to re-enter the industry).[73]

With respect to our finding that Leverett violated Conduct Rules 2110 and 3110 by reviewing and approving false records, we have considered Leverett's false and evasive responses about the extent of his involvement in the falsification of the ASWI order tickets to be an aggravating factor. We also consider Leverett's reviewing and approving false tickets to be egregious conduct and thus have

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[71] In fashioning sanctions, the Hearing Panel consulted the Guideline for failure to respond (Guideline (1998 ed.) at 31), which provides that a bar should be standard and that fines should range between $25,000 and $50,000.

[72] See Guidelines (1998 ed.) at 28.

[73] See note 46 above.

looked to the upper end of the range of sanctions under the recordkeeping Guideline. Therefore, we impose a suspension of one year from associating with any member firm in any capacity and a fine of $10,000 (such fine is suspended until such time as Leverett may seek to re-enter the industry).[74]

F. Supervisory Failures

Conduct Rule 3010(b)(1) requires member firms to establish, maintain and enforce written supervisory procedures that are reasonably designed to achieve compliance with applicable laws, rules and regulations. The Commission has stated that "[r]ed flags and suggestions of irregularities demand inquiry as well as adequate follow-up and review. When indications of impropriety reach the attention of those in authority, they must act decisively to detect and prevent violations of the federal securities laws." In re Edwin Kantor, 51 S.E.C. 440, 447 (1993).

1. Montelbano Failed to Supervise Properly. The Hearing Panel found that Montelbano, as Monitor's acting president, had taken no action to detect, prevent or remedy the sales practice abuses detailed above despite the existence of red flags and suggestions of irregularities. Montelbano argued that he was not acting as president during the relevant period and that he did not become president of Monitor officially until June 1996, after the manipulation in ASWI had occurred. The evidence in the record supports the Hearing Panel's findings and does not support Montelbano's contention.

Montelbano had held himself out as president of Monitor to NASD staff as early as April 3, 1996, and on numerous occasions thereafter.[75] Further, a number of Monitor brokers testified either that Montelbano was the president of Monitor or that he was their supervisor and had hired them. Sharon Feliciano ("Feliciano"), who assisted Monitor's operations director, stated during her on-the-record interview that Montelbano was a supervisor at Broad Street and that she had brought certain

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[74] The Hearing Panel imposed no sanctions on Leverett under cause 17 because it dismissed that cause.

[75] Wayne Freeman, an NASD staff supervisor, testified that on April 3, 1996, the first date that he visited the Firm as part of his examination, Montelbano introduced himself as the president of Monitor. Thereafter, NASD sent multiple requests for documents to Montelbano, as president of Monitor, throughout April and May 1996 (dated April 19, 1996, April 23, 1996, and May 7, 1996 (two separate requests). Freeman also testified that, subsequent to Montelbano's receipt of the NASD's April 23, 1996 request for documents, Montelbano advised him to direct any further written requests for documents to him. Shields, one of the NASD examiners who investigated Monitor's trading in ASWI shares, testified that during his visits to Monitor in April and May 1996, Montelbano held himself out as the Firm's president. We note that a few brokers testified that they thought that Palla was the president of Monitor. While Palla may have been president of Monitor at one time, the credible evidence of record establishes that Montelbano held himself out and acted as president before, during, and after the ASWI distribution on May 13-14, 1996.

issues to his attention, such as the fact that an unregistered representative employed by the Firm was conducting a securities business. Feliciano also testified that Montelbano was the individual that the Monitor brokers would go to when they had a problem.

The evidence shows that Montelbano, in his capacity as president of Monitor, failed to supervise Monitor brokers when confronted with evidence of red flags regarding irregularities with respect to Monitor's distribution of ASWI shares to the public.[76] In In re John H. Gutfreund, 51 S.E.C. 93, 111 (1992), the Commission found that the president of Salomon Brothers Inc. was responsible for the operations of Salomon and that he had failed to discharge his supervisory responsibilities with respect to misconduct by a Salomon broker that had come to his attention. The Commission has noted that the president of a broker-dealer "is responsible for compliance with all of the requirements imposed on his firm unless and until he reasonably delegates particular functions to another person in that firm, and neither knows nor has reason to know that such person's performance is deficient." In re Universal Heritage Investments Corp., 47 S.E.C. 839, 845 (1982).

Montelbano admitted that he thought something was wrong when Monitor brokers informed him that ASWI had started trading on May 13, 1996, nevertheless, he remained with Monitor even after NASD examiners had met with certain Monitor employees on May 16, 1996 and asked questions about the trading that had occurred in ASWI on May 13-14, 1996. In fact, NASD registration records show that Montelbano remained with Monitor until July 1996. Despite these red flags about problems with the trading that had occurred in ASWI on May 13-14, 1996, Montelbano did nothing. We find that Montelbano's inaction constituted a failure to supervise properly. We therefore affirm the Hearing Panel's finding under cause 21 that Montelbano violated Conduct Rules 2110 and 3010.

2. Leverett Failed to Supervise Properly. We called this matter for review in part to analyze the Hearing Panel's findings and sanctions under cause 23. The Hearing Panel found that Leverett was the only registered general securities principal at the Third Avenue office on May 13-14, 1996, and that he had violated Conduct Rule 2110 and 3010 by taking no action to detect, prevent, or remedy the manipulative trading of ASWI shares, and by reviewing and approving the ASWI order tickets with excessive mark-ups and more than 50 order tickets that had been canceled and rebilled on May 16, 1996 with lower sales credits.

The Hearing Panel did not credit Leverett's testimony that he did not recall the ASWI tickets' having been canceled and rebilled and that he was sure he had not been involved in the process. Nor did the Hearing Panel credit Leverett's testimony that he was sure that when he signed the order tickets

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[76] Montelbano's immediate response bordered on abandonment. Montelbano testified that he was surprised when ASWI began trading on May 13, 1996, and that in response to this development, he and McMahon left the office at about 11:00 a.m. on May 13, 1996 to meet with a headhunter about possible employment at another firm.

there had been only a limit price on each ticket (not a reported or executed price), with no mark-ups. As discussed above, we adopt this finding. We also agree with the Hearing Panel's conclusion that the number of cancels and rebills alone was a sufficient red flag or suggestion of irregularity to require inquiry, follow-up, and review. Leverett, however, took no action. The fact that Leverett was one of the principals who met with NASD officials on May 16, 1996 about the ASWI trades that Monitor had executed on May 13-14, 1996 is further evidence that Leverett was aware of possible problems with the ASWI trades when he reviewed and approved the cancels and rebills for those trades on May 16, 1996. Accordingly, we affirm the Hearing Panel's finding that Leverett violated Conduct Rules 2110 and 3010.

3. Sanctions for Supervision Violations. The Guideline for failure to supervise recommends suspending the responsible individual in all supervisory capacities for up to 30 days and a fine in the range of $5,000 to $50,000.[77] Montelbano was Monitor's acting president during the relevant period, yet there is no evidence in the record that he made any effort to implement any supervisory system or controls. In fact, as the Hearing Panel found, Monitor's business operations were "pretty much a free-for-all," with no oversight whatsoever. As noted in our discussion of the violations above, Montelbano and Leverett each ignored red flags that indicated that there were irregularities with respect to the sale of ASWI shares to Monitor's customers. We agree with the Hearing Panel that the end result of Montelbano's and Leverett's abandonment of their responsibilities was that a massive fraud was perpetrated on the investing public.

We called this matter for review in part to determine whether the findings and sanctions as to Leverett were appropriate. We find that the sanctions that the Hearing Panel imposed on him are appropriate. As the Hearing Panel found, Leverett had far less responsibility than Montelbano, who was the acting president of Monitor, and Leverett had been a general securities principal for only about six days when the trading in ASWI shares commenced on May 13, 1996. The Hearing Panel imposed on Leverett a suspension of 45 business days, and a $5,000 fine (with the fine suspended until such time as he may seek to re-enter the securities industry), and a requalification requirement to run concurrent with the 45-day suspension.[78] We find that these sanctions are appropriately remedial.[79]

As to Montelbano, the Hearing Panel imposed a fine of $10,000 (suspended until such time as Montelbano may seek to re-enter the securities industry) and barred Montelbano from associating with

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[77] See Guideline (1998 ed.) at 89.

[78] See note 46 above. We order Leverett to requalify as a general securities representative by passing the Series 7 within 90 days of the date this decision and to requalify as a general securities principal by taking the Series 24 examination within 180 days of the date of this decision.

[79] We modify the requalification requirement by ordering that the periods within which Leverett must requalify will be determined from the date of issuance of this decision.

any member firm in any capacity.[80] We agree with the imposition of these sanctions and find that they are appropriately remedial and in the public interest.

G. Failure to Respond Truthfully to NASD Regulation Inquiries

Procedural Rule 8210 requires a member, person associated with a member, or person subject to the Association's jurisdiction to provide information orally, in writing, or electronically in response to requests from NASD staff in connection with an investigation, complaint, examination, or proceeding authorized by the NASD By-Laws or the Rules of the Association. The requirement to respond truthfully to NASD inquiries is subsumed in the legal principles in Rule 8210. Rules 8210 and 2110 are violated when an associated person's statements are untruthful.[81]

1. Galasso Failed to Respond Truthfully to an NASD Regulation Request for Information. During the investigation, Galasso testified that on May 13, 1996, he received an order for 10,000 shares of ASWI from Magelinsky on behalf of Ernst, but Magelinsky denied during her hearing testimony that she had ever placed such an order. Yvonne Huber, one of the NASD examiners who investigated this case, testified, however, that Ernst did have a 10,000 share order to purchase ASWI, but she had no information about whether Magelinsky ever purchased the full order. There is no documentary evidence in the record that Magelinsky ever placed an order for 10,000 shares. Based on the conflicting evidence regarding this allegation, we find that there is insufficient evidence that Galasso testified untruthfully about whether he had received a 10,000 share order from Magelinsky for ASWI during the relevant period.

Galasso further testified during an on-the-record interview that he did not know a "Mr. and Mrs. DeFazio." Galasso's first sales of ASWI on May 13, 1996 were to Monarch Financial for the account of the DeFazios. Galasso admitted at the hearing that the DeFazios were his grandparents and

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80 See note 46 above.

81 See In re Jawahar Doshi, Complaint No. C10960047 (NAC Jan. 20, 1999) (NAC finding that 8210 and 2110 violations occurred where respondent told staff during on-the-record interview that voice on customer's tape recording was not his but later admitted it was his voice); In re Mark Shear, Complaint No. C9A950055 (NBCC Jan. 24, 1997) (NAC finding that 8210 and 2110 violations occurred where respondent denied knowledge of exam impostor's identity during an 8210 interview, but later admitted friendship with impostor in addition to record showing that the two were acquaintances); In re John Gordon Nevers, Complaint No. C3A93009 (NBCC May 13, 1994) (NAC finding that 8210 and 2110 predecessor rule violations where respondent advised staff that he did not deposit customer checks in his personal account, but bank documentation showed he did); In re Brian L. Gibbons, 52 S.E.C. 791 (1996), aff'd, 112 F.3d 516 (9th Cir.1997) (table format) (holding that where NASD inquired about respondent's compensation and respondent stated that he made no financial gain but later conceded that he was paid, Rule 8210's predecessor rule was violated).

that he had not told the truth at the on-the-record interview. Based on the evidence of Galasso's inconsistent statements and his admission, we conclude that there is ample evidence that he failed to respond truthfully to NASD inquiries during his on-the-record interviews.

On the other hand, we find no evidence, based on the excerpts that were included in the record of Galasso's on-the-record testimony, that he failed to respond truthfully during the course of his on-the-record interviews about the following issues, as also alleged in cause 35 of the complaint: (1) the way orders for ASWI were entered at Monitor on May 13-14, 1996; (2) the methods by which prices charged to customers and compensation intended to be paid to brokers for purchases of ASWI were determined at Monitor; and (3) his knowledge about entities whose purchases of ASWI effected an upward price move. Based on the insufficiency of the evidence, we dismiss these allegations.[82]

We thus reverse the Hearing Panel's finding under cause 35 that Galasso violated Rules 2110 and 8210 as to the statement he made about Magelinsky placing an order for 10,000 shares, and dismiss that allegation and the other statements as noted above with respect to cause 35. We affirm the Hearing Panel's finding that Galasso made an untruthful statement about whether he knew his grandparents and find that Galasso violated Rules 2110 and 8210 as to that statement.

2. McMahon Failed to Respond Completely and Truthfully to NASD Regulation Requests for Information. The Hearing Panel found that McMahon had failed to respond completely and truthfully during his on-the-record interview about his knowledge of and involvement in the marketing of ASWI. First, although McMahon testified that he had first heard about ASWI in March 1996 when Pokross introduced him to Tagliareni, Tagliareni contradicted that statement, testifying that he had first met McMahon prior to his association with Monitor in September 1995. McMahon continued to insist during the hearing that he had first met Tagliareni during the first quarter of 1996.

Second, McMahon stated during his on-the-record interview that the only conversation he had with Montelbano about ASWI prior to May 1996 was to tell Montelbano that Tagliareni was a nice guy. This statement was refuted by Montelbano's testimony that McMahon had introduced him to Tagliareni in November 1995 and that McMahon had told him during that meeting with Tagliareni that Monitor might be doing some business with ASWI. Montelbano also testified that McMahon subsequently gave him a business plan for ASWI to review and told him that ASWI was not going be an IPO but was going to be a Rule 504 placement.

Third, McMahon testified throughout his on-the-record interview and at the hearing that he had never spoken to Monitor brokers about ASWI prior to May 13, 1996. Contrary to McMahon's

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[82] The Hearing Panel did not make any findings on these allegations.

statement, the record includes overwhelming evidence that McMahon spoke to Monitor brokers on several occasions about ASWI prior to the commencement of trading on May 13, 1996.[83]

We credit Tagliareni's and Montelbano's testimony and the Monitor brokers' testimony over McMahon's because McMahon's statements were contradicted by the great weight of evidence, as detailed above.[84] We also find that McMahon failed to respond truthfully to NASD Regulation staff's questions about price forecasts he made with respect to ASWI and the pricing of ASWI, as alleged in the complaint, by denying that he had ever discussed these issues with Monitor brokers.[85] As noted above in our discussion of the ASWI manipulation, Monitor brokers refuted McMahon's denials that he had ever discussed ASWI with them prior to the commencement of trading on May 13, 1996. We thus find under cause 34 that McMahon violated Rules 8210 and 2110 by failing to respond to NASD inquiries completely and truthfully.

3. Montelbano Failed to Respond Completely and Truthfully to NASD Regulation Requests for Information. Cause 33 alleged that Montelbano was untruthful about three issues. The Hearing Panel found that Montelbano failed to respond completely and truthfully during his on-the-record interview regarding his knowledge of Pokross' interest in stocks that Monitor was selling to its customers and his knowledge of Pokross' financial interest in the Firm. We find the record insufficient to support this conclusion.

The Hearing Panel also found that Montelbano was not truthful about his own activities concerning the marketing of ASWI, since his statements denying any involvement in the marketing of ASWI were rebutted by the testimony of Monitor brokers from the Broad Street office who stated in their on-the-record interviews that Montelbano had told them about ASWI. We find substantial evidence in the record to support this finding.

Additionally, we find that Montelbano failed to respond truthfully to NASD Regulation staff questions about his role in the day-to-day operations of Monitor.[86] Although certain brokers testified

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83 See discussion above on pp. 13-15.

84 The Hearing Panel did not make any credibility determinations with respect to the conflicting testimony. With respect to our credibility findings, there is no evidence to suggest that Montelbano, Tagliareni, or the other brokers had any particular bias against McMahon, nor is there any record evidence that contradicts our general credibility findings.

85 The Hearing Panel's decision did not address these allegations in cause 34 of the complaint.

86 The Hearing Panel's decision did not address this particular allegation.

that Palla was the president of Monitor, the great weight of the evidence indicates that Montelbano acted as Monitor's president during the relevant period.[87]

Accordingly, we affirm the Hearing Panel's finding that Montelbano failed to respond completely and truthfully about his activities with respect to the marketing of ASWI, and we find that he was untruthful about his role in the day-to-day operation of Monitor, in violation of Rule 2110 and 8210. We reverse that part of the Hearing Panel's decision that found Montelbano in violation of Rule 8210 and 2110 regarding his knowledge of the involvement of Pokross in the day-to-day activities of Monitor.

4. There is Insufficient Evidence to Find that Nejaime Failed to Respond Truthfully to Requests for Information. We called this matter for review in part to review the appropriateness of the findings and sanctions that the Hearing Panel imposed against Nejaime under cause 41 of the complaint, which alleged that Nejaime had failed to testify truthfully at his on-the-record interview about his activities with respect to the marketing and coordination of the ASWI "offering" and his role in the management of the 919 Third Avenue office.

The Hearing Panel found that Nejaime had failed to testify truthfully because he testified at hearing that he did not know why all of the ASWI transactions for his customers had been executed at the same price even though he had admitted at his on-the-record interview that McMahon had told him the price at which ASWI would be available. We find that even though Nejaime might not have testified truthfully at the hearing, he had testified truthfully at the on-the-record interview. We note that he was only charged with testifying untruthfully at his on-the-record interview. Accordingly, we reverse the Hearing Panel's finding of violation in this regard.

The Hearing Panel also found that Nejaime failed to respond truthfully when he denied receiving commissions on the ASWI trades that he effected for his customers. The Hearing Panel reached this conclusion because Nejaime and another Monitor broker, Kevin Radigan ("Radigan") shared a joint registered representative number and Radigan was compensated for the periods May 20 to June 17, 1996 and June 20 to July 15, 1996 (which compensation included Nejaime's seven ASWI customer transactions). We reverse because, notwithstanding the evidence that Radigan received commissions on the ASWI trades that Nejaime effected, the record contains no evidence that Nejaime received any of those commissions. In fact, Nejaime expressed displeasure during his hearing testimony about not having received any of those commissions from Radigan.

The Hearing Panel also found insufficient evidence to prove that Nejaime had made a number of other untruthful statements during his on-the-record interview, as alleged in cause 41. We concur with

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[87] See discussion above on pp. 35-36.

the Hearing Panel's determination and adopt its findings as to these other statements as detailed in the Hearing Panel's decision.

In sum, we reverse the Hearing Panel's finding that Nejaime violated Rules 8210 and 2110 with respect to: (1) statements he made about his understanding of the price at which his customer orders were executed; and (2) statements he made about whether or not he had received commissions on his customer transactions for the ASWI trades. We affirm the Hearing Panel's decision that there was insufficient evidence to find that Nejaime had made a number of other untruthful statements, as detailed in the Hearing Panel's decision. We also find no evidence that Nejaime failed to respond truthfully at his on-the-record interview regarding his role in the management of the Third Avenue office, as alleged in the complaint.[88] Having found that Nejaime did not violate Rules 8210 and 2110, we dismiss the allegations in cause 41 of the complaint that Nejaime provided untruthful testimony in response to inquiries from the NASD.

5. Leverett Failed to Testify Truthfully In Response to Requests for Information. The Hearing Panel determined under cause 42 that on two occasions during his on-the-record interview, Leverett failed to respond truthfully to NASD inquiries regarding ASWI order tickets. The Hearing Panel determined that although Leverett testified during his on-the-record interview that mark-ups were disclosed on his customers' confirmations for their purchases of ASWI, the customer confirmations at issue reflected no mark-ups or commissions. In addition, the Hearing Panel found that Leverett stated during this interview that he had not seen a mark-up higher than $1, notwithstanding that order tickets that bore his initials (indicating that he had reviewed and approved those tickets) reflected mark-ups ranging from $1 to $2.25. We affirm the Hearing Panel's finding that Leverett violated Rules 8210 and 2110. We dismiss the remaining allegations as to Leverett set forth in cause 42 that the Hearing Panel did not address based on a lack of evidence in the record to support a finding of violation.[89]

6. Sanctions for Failure to Respond Truthfully Violations

The Guideline relevant to the aforementioned violations recommends a fine of $25,000 to $50,000 for failure to respond and failure to respond truthfully and a fine of $10,000 to $25,000 for failure to respond completely.[90] The Guideline states that a bar should be standard if the individual did

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88 The Hearing Panel did not address this allegation in the complaint.

89 The complaint alleged that Leverett failed to respond truthfully at his on-the-record interview about the following: (1) the order, origin and the nature of tickets he reviewed and approved for trades involving ASWI; (2) his role in reviewing documents as a supervising principal in the Third Avenue office; and (3) the creation of fraudulent order tickets intended to deceive the staff about transactions in ASWI. The excerpts of Leverett's on-the-record testimony that were included in the record did not support these allegations.

90 See Guidelines (1998 ed.) at 31.

not respond in any manner, and where mitigation exists, or the person did not respond timely, consider suspension of up to two years.

We have found that Galasso, McMahon, Montelbano, and Leverett each provided false testimony during their respective on-the-record interviews concerning the events associated with the ASWI scheme. In determining sanctions, we have considered that at the point that the information was requested by NASD Regulation staff, it was of regulatory significance because NASD Regulation was investigating whether misconduct had occurred, by whom, and to what extent. Further, like the Hearing Panel, we have considered the type of information withheld or misrepresented, the circumstances surrounding each respondents' on-the-record interview, the clarity of the questions asked, and the respondents' experience in the securities industry.

As to Galasso, the Hearing Panel imposed a suspension of one year and a fine of $30,000 (suspended until such time as he attempts to re-enter the securities industry). We have determined to reduce the period of suspension to 10 business days and to reduce the fine to $1,000 (the fine is suspended until such time as Galasso may seek to re-enter the securities industry).[91] In reaching these sanctions, we considered that Galasso testified falsely as to one area in his on-the-record interview, and that contrary to the other respondents in this matter he eventually, albeit under the compulsion of a complaint and hearing, admitted the truth.[92]

We affirm the Hearing Panel's decision to suspend McMahon and Montelbano for a period of two years from associating with any member firm in any capacity, respectively. We also affirm the Hearing Panel's imposition of a $40,000 fine on McMahon and a $40,000 fine on Montelbano (the fines are suspended until such time as respondents may seek to re-enter the securities industry).[93] In deciding to affirm these sanctions, we considered that McMahon's and Montelbano's untruthful testimony interfered materially with the NASD's investigation of the manipulation of ASWI shares during the relevant period, and that the sanctions are therefore appropriately remedial.

The Hearing Panel imposed on Leverett a suspension of 30 business days from associating with any member firm in any capacity and a fine of $1,000 (suspended until such time as he may seek to re-enter the securities industry). We have determined to increase the sanctions against Leverett to a one-year suspension and $10,000 fine (suspended until such time as he may seek to re-enter the securities

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91 See note 46 above.

92 It is also for this reason that we have decided to impose a fine below the $25,000 to $50,000 range recommended in the Guidelines for failure to testify or failure to testify truthfully.

93 See note 46 above.

industry).[94] In reaching this determination, we considered that Leverett's failure to testify truthfully about the ASWI order tickets impacted the NASD's ability to investigate an important part of the scheme -- Monitor's attempt to lower the prices and mark-ups that had been charged on May 13-14, 1996, through the creation of bogus trades that were made on May 16, 1996, but which were back-dated to May 13-14, 1996.

III. Summary of NAC Findings and Sanctions

We have made the following findings as to liability as to each respondent with respect to each of the causes alleged in the complaint:

Galasso

- Manipulation (Cause Seven): We affirm the Hearing Panel's findings that Galasso, as the Firm's sole trader, manipulated ASWI shares on May 13-14, 1996, in violation of Section 10(b), Rule 10b-5, and Conduct Rules 2110 and 2120;

- Excessive and Fraudulent Mark-Ups (Cause 15): We affirm the Hearing Panel's finding that Galasso violated Conduct Rules 2110, 2120, and 2440, and Section 10(b) and Rule 10b-5. We find that Galasso knew that the Firm dominated and controlled the market for the ASWI shares and that customers would be charged excessive mark-ups if those mark-ups were not based on the Firm's contemporaneous cost;

- Rule 10b-6 (Cause 16): We affirm the Hearing Panel's finding of violation, but on a basis that differs from that of the Hearing Panel. We find that Galasso violated Rule 10b-6 and 2110 and 2120, and Section 10(b) and Rule 10b-5;

- False and Fictitious Records and Alleged Failure to Provide Order Tickets (Cause 18): We affirm the Hearing Panel's finding that Galasso violated Conduct Rules 2110 and 3110, by assisting in the creation of false trade confirmations by ensuring that the same limit price, reported price, and execution price were the same on all the order tickets. We reverse the Hearing Panel's finding that Galasso violated Rule 8210 by submitting an incomplete set of order tickets in response to an NASD Rule 8210 request on the basis that the complaint did not allege that the NASD had directed a request for the original order tickets to Galasso. We therefore dismiss the Hearing Panel's finding of violation as to Rule 8210; and

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[94] See note 46 above. We have determined that it is appropriate to impose a fine below the $25,000 to $50,000 range recommended by the relevant Guideline because of our belief that the sanctions as a whole are sufficiently remedial.

$ Failure to Testify Truthfully (Cause 35): We affirm the Hearing Panel's finding that Galasso violated Rules 8210 and 2110 by providing untruthful answers on one matter. In addition, we dismiss the other allegations in this cause of the complaint not addressed by the Hearing Panel.

McMahon

$ Manipulation (Cause Five): We affirm the Hearing Panel's finding that McMahon violated Section 10(b), Rule 10b-5, and Conduct Rules 2110 and 2120 by participating in the manipulation of ASWI shares;

$ Rule 10b-6 (Cause 16): We reverse the Hearing Panel's finding that McMahon violated Rule 10b-6, Conduct Rules 2110, 2120, and Section 10(b) and Rule 10b-5; and

$ Failure to Respond Truthfully and Completely (Cause 34): We affirm the Hearing Panel's finding that McMahon violated Rules 8210 and 2110 by failing to respond to NASD inquiries completely and truthfully about three topics. In addition, we find that he was untruthful as to an additional matter not addressed by the Hearing Panel.

Montelbano

$ Manipulation (Cause Four): We affirm the Hearing Panel's findings that Montelbano violated Section 10(b), Rule 10b-5, and Conduct Rules 2120 and 2110 by participating in the manipulation;

$ Rule 10b-6 (Cause 16): We reverse the Hearing Panel's finding that Montelbano violated Rule 10b-6, Conduct Rules 2110, 2120, and Section 10(b) and Rule 10b-5;

$ Supervision (Cause 21): We affirm the Hearing Panel's finding that Montelbano violated Conduct Rules 2110 and 3010 for failure to supervise by failing to respond to red flags in connection with the trading of ASWI shares in his capacity as acting president of Monitor during the relevant period; and

$ Failure to Testify Truthfully and Completely (Cause 33): We affirm the Hearing Panel's finding that Montelbano violated Rules 8210 and 2110 by failing to respond completely and truthfully about one matter, but we reverse the Hearing Panel's finding that he was untruthful about a second. In addition, we find that he was untruthful about another matter not addressed by the Hearing Panel.

Leverett

$ Manipulative and Deceptive Trading Practices (Cause 13): We affirm the Hearing Panel's determination that the record contained insufficient evidence that Leverett made certain misrepresentations to two of his customers. We reverse the Hearing Panel's additional findings because the complaint failed to allege these violations. We therefore dismiss the allegation that Leverett violated Section 10(b) and Rule 10b-5, and Conduct Rules 2120 and 2110 as alleged in this cause;

$ False and Fictitious Records (Cause 17): We reverse the Hearing Panel's dismissal of the allegations as to Conduct Rules 3010 and 2110, and we find that Leverett violated those rules by reviewing and approving falsified order tickets. We affirm the Hearing Panel's dismissal of the allegations as to Conduct Rule 8210, but we do not adopt the Hearing Panel's rationale for dismissal;

$ Supervision (Cause 23): We affirm the Hearing Panel's decision that Leverett violated Conduct Rule 2110 and 3010 by taking no action in response to red flags, in his capacity as the only principal at Monitor's Third Avenue office; and

$ Failure to Respond Truthfully (Cause 42): We affirm the Hearing Panel's finding that Leverett violated Rules 8210 and 2110 by failing to respond truthfully to questions during his on-the-record interview. We dismiss the remaining allegations not addressed by the Hearing Panel for lack of evidence.

Nejaime

$ Manipulative and Deceptive Trading Practices (Cause 14): We reverse the Hearing Panel's finding that Nejaime engaged in manipulative and deceptive trading practices in violation of Section 10(b), Rule 10b-5, and Conduct Rules 2110 and 2120; and

$ Failure to Testify Truthfully (Cause 41): We reverse the Hearing Panel's finding that Nejaime violated Rules 8210 and 2110 with respect to statements he made about two matters. We affirm the Hearing Panel's decision that there was insufficient evidence to find that Nejaime had made a number of other untruthful statements, as detailed in the Hearing Panel's decision. We find no evidence that Nejaime failed to respond truthfully at his on-the-record interview regarding another matter which the Hearing Panel did not address. We therefore dismiss the allegations in cause 41 of the complaint that Nejaime provided untruthful testimony in response to inquiries from the NASD.

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The following is a summary of the sanctions we have imposed for each respondent, by violation:

Galasso

$ Manipulation (Cause Seven): a bar from associating with any member firm in any capacity and a fine of $50,000 (the fine is suspended until such time as Galasso may seek to re-enter the securities industry);

$ Excessive Mark-Ups (Cause 15): a bar from associating with any member firm in any capacity and a fine of $30,000 (the fine is suspended until such time as Galasso may seek to re-enter the securities industry);

$ Rule 10b-6 (Cause 16): the sanction we imposed for the manipulation violation (cause seven) also is applicable to Galasso's violation of Rule 10b-6;

$ False and Fictitious Records (Cause 18): a suspension for one year from associating with any member firm in any capacity and a fine of $10,000 (the fine is suspended until such time as Galasso may seek to re-enter the securities industry; and

$ Failure to Respond Truthfully (Cause 35): a suspension for 10 business days from associating with any member firm in any capacity and a fine of $1,000 (the fine is suspended until such time as Galasso may seek to re-enter the securities industry).

In summary, Galasso is barred from associating with any member firm in any capacity, suspended for a period of one year, plus 10 business days, from associating with any member firm in any capacity, and fined a total amount of $91,000 (the fine to be suspended until such time as he may seek to re-enter the securities industry).

McMahon

$ Manipulation (Cause Five): a bar from associating with any member firm in any capacity and a fine of $50,000 (the fine is suspended until such time as McMahon may seek to re-enter the securities industry); and

$ Failure to Respond Truthfully and Completely (Cause 34): a suspension of two years from associating with any member firm in any capacity and a $40,000 fine (the fine is suspended until such time as respondent may seek to re-enter the securities industry).

In summary, McMahon is barred from associating with any member firm in any capacity, suspended for a period of two years from associating with any member firm in any capacity, and fined a

total amount of $90,000 (the fine to be suspended until such time as he may seek to re-enter the securities industry).

Montelbano

$ Manipulation (Cause Four): a bar from associating with any member firm in any capacity and a $40,000 fine (the fine is suspended until such time as Montelbano may seek to re-enter the securities industry);

$ Failure to Supervise Properly (Cause 20): a bar from associating with any member firm in any capacity and a fine of $10,000 (the fine is suspended until such time as Montelbano may seek to re-enter the securities industry); and

$ Failure to Respond Truthfully and Completely (Cause 33): a suspension of two years from associating with any member firm in any capacity and a $40,000 fine (the fine is suspended until such time as Montelbano may seek to re-enter the securities industry).

In summary, Montelbano is barred from associating with any member firm in any capacity, suspended for a period of two years from associating with any member firm in any capacity, and fined a total amount of $90,000 (the fine to be suspended until such time as he may seek to re-enter the securities industry).

Leverett

$ False and Fictitious Records (Cause 17): a suspension of one year from associating with any member firm in any capacity and a fine of $10,000 (the fine is suspended until such time as Leverett may seek to re-enter the securities industry);

$ Failure to Supervise (Cause 23): a suspension of 45 business days in any capacity and a $5,000 fine (the fine suspended until such time as Leverett may seek to re-enter the securities industry), and a requalification requirement as a general securities principal and a general securities representative,[95] to run concurrent with the 45-day suspension; and

$ Failure to Testify Truthfully (Cause 42): a suspension of one year from associating with any member firm in any capacity and a fine of $10,000 (the fine is suspended until such time as Leverett may seek to re-enter the securities industry).

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[95] We order that Leverett requalify as a general securities representative by passing the Series 7 within 90 days of the date of this decision and that he requalify as a general securities principal by taking the Series 24 examination within 180 days of the date of this decision.

In summary, Leverett is suspended for two years, plus 45 business days, from associating with any member firm in any capacity; required to requalify by examination as a general securities representative and general securities principal as set forth in note 91, supra, and fined a total amount of $25,000 (the fine to be suspended until such time as he may seek to re-enter the securities industry).

The costs of the hearing below, $25,349.00 ($24,599.00 for transcripts and $750 administrative fee), are assessed jointly and severally against McMahon, Montelbano, and Galasso. The bars that have been imposed are effective immediately upon the issuance of this decision.[96]

On Behalf of the National Adjudicatory Council,

Joan C. Conley, Senior Vice President and Corporate Secretary

[96] Because Galasso, McMahon, and Montelbano have each been barred in all capacities, no commencement date for their respective suspensions will be designated.

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.